

**VILLAGE BANKS, *CAISSES VILLAGEOISES*, AND CREDIT UNIONS:
LESSONS FROM CLIENT-OWNED MICROFINANCE ORGANIZATIONS
IN WEST AFRICA**

by

Korotoumou Ouattara

Claudio Gonzalez-Vega

and

Douglas H. Graham

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Rural Finance Program
Department of Agricultural, Environmental, and Development Economics
The Ohio State University
2120 Fyffe Road
Columbus, Ohio 43210-1099
rurfin@postbox.acs.ohio-state.edu

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VILLAGE BANKS, *CAISSES VILLAGEOISES*, AND CREDIT UNIONS: LESSONS FROM CLIENT-OWNED MICROFINANCE ORGANIZATIONS IN WEST AFRICA¹

Korotoumou Ouattara, Claudio Gonzalez-Vega, and Douglas H. Graham²

I

INTRODUCTION

A. Rationale and Objectives

This case study is a component of the research project on *Client-Owned Microfinance Organizations: Lessons from West Africa*, conducted by the Rural Finance Program at The Ohio State University (OSU) under the Microfinance Best Practices (MBP) Program. The main objective of the study has been to assess the strengths and weaknesses of *mutualist* financial organizations in the delivery of microfinance services, both loans and deposit facilities, in comparatively poor countries.

The common thread that binds several types of *mutualist* financial organizations is that they are client-owned institutions. Some of them are financial cooperatives developed along traditional credit union designs, others are village banking systems sponsored by international non-governmental

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² Ouattara, now at The World Bank, was a Research Specialist until April 1998 and Gonzalez-Vega and Graham are Professors in the Department of Agricultural, Environmental, and Development Economics at The Ohio State University (OSU). Gonzalez-Vega is also Director of the Rural Finance Program at OSU. The authors are particularly grateful with Barbara McNelly, Peggy Roark, and her colleagues at Freedom from Hunger, for their extensive comments on earlier drafts, with Renée Chao-Béroff at the Centre International de Développement et de Recherche (CIDR), for her support of their earlier research in West Africa, and with Thomas Shaw (PIEC Savings and Credit Program), for his guidance in Mali. Geneviève Nguyen and Mayada Baydas were contributors to the earlier OSU research in the region. Robin Young (DAI) and Annica Jensen (USAID) have been patient managers of the project. This exercise would not have been possible without the assistance and warm hospitality of officers and clients of the programs visited, as listed in Annex A. Lori Kam was, as always, helpful with the word processing.

organizations (NGOs), and still others are village-owned savings and credit associations, including the *caisses villageoises* that operate in several African countries.

The *caisses villageoises* model discussed here was designed by a French NGO, the *Centre International de Développement et de Recherche* (CIDR), and key elements observed in informal village organizations were adopted in the design.³ This model was first implemented in the mid-1980s in Burkina Faso, and it is now found in Mali, The Gambia, Niger, Madagascar, Ethiopia, and Sao Tomé et Príncipe.⁴ This MBP case study compares these *caisses villageoises* with two other distinct types of client-owned organizations, which have been providing microfinance services to poor clients in West Africa.

One of these alternative organizational designs are the financial cooperatives or credit unions, which have been developed in West Africa primarily through the auspices of The World Council of Credit Unions (WOCCU) and the Canadian organization *Développement International Desjardins* (DID). The other type of organizational design are the village banking systems developed from the original model of FINCA International and sponsored in West Africa, with important adaptations, by US-based NGOs such as Catholic Relief Services (CRS), Freedom from Hunger, and Save the Children.

The present case study conducts a preliminary comparative analysis of these three institutional forms. There are several advantages of undertaking a comparative analysis. The comparison makes it possible to identify some common threads that may explain the success or failure of this type of organizations as well as common factors that may generally facilitate or limit their future expansion.

The identification of common features shared by all types of client-owned organizations can enrich a discussion about the challenges faced by organizations with similar structures of property rights and with the resulting governance mechanisms. The effort to derive some stylized facts common to all of these types of organizations has carried the danger, however, that some of the differentiating features may have been missed by the researchers.⁵

The observation of differences in the performance of alternative varieties of the client-owned institutional model makes it possible, nevertheless, to rank these diverse attempts to address the

³ The term *caisses villageoises* is used extensively in West Africa to designate various types of mutualist organizations. The terms *caisse populaire* and *caisse locale* are also common. The term *caisses villageoises* is used here in the narrow sense of the model developed by CIDR.

⁴ For an in-depth analysis of the *caisses villageoises* in Mali, see Ouattara, Nguyen, Gonzalez-Vega and Graham (1997) and Gonzalez-Vega, Nguyen, and Outtara (1998).

⁵ The researchers are aware that, in their attempt to build a stylized model of these institutions, they may not always do full justice to particular organizations and to the adjustments that they have adopted. The purpose of the case study, however, was not to evaluate specific organizations but to derive lessons of general interest.

challenges posed by mutualist institutions according to their apparent effectiveness. The final objective of the research project is to derive lessons to be used by village banking organizations in their efforts to evolve into large-scale, fully sustainable financial intermediaries.

The analysis of this case study is a first attempt to look at the comparative performance of mutualist organizations in low income countries and, by necessity, it focuses on broad features of these organizations. A more detailed analysis would be needed to evaluate the performance of the individual organizations observed here to illustrate the questions addressed by the study. Such an evaluation of individual performance was not the purpose of the case study and it is not accomplished here, in part due to the limitation of the resources available and in part due to the short visits to the organizations. The objective, instead, has been to derive some specific lessons of general interest from a brief observation of these experiences.

Moreover, this case study does not rank mutualist versus non-mutualist organizations and does not discuss the advantages and disadvantages of alternative structures of property rights. This is an important question, however, because an organization's performance is the result of decisions influenced by incentives that emerge, in turn, from the structure of property rights of the organization. Many microfinance organizations suffer from structures of attenuated property rights (lack of well-defined owners), which threaten their sustainability.

B. Conceptual Issues

The theoretical literature has amply discussed advantages and disadvantages of *mutualist* financial organizations, and empirical evidence on their costs and benefits has been collected on financial cooperatives (Flannery, 1974; Smith *et al.*, 1981; Poyo, 1986).

The benefits of mutualist organizations emerge from their information and contract enforcement advantages (Poyo, Gonzalez-Vega, and Aguilera-Alfred, 1992; Shaw, 1995). Members of a small credit union, for example, can use their stock of knowledge about other individual members in screening and monitoring borrowers and can mobilize peer pressure for the enforcement of contracts. Voluntary work can be used to run the organization and to monitor its performance.

The disadvantages of these organizations emerge from their ownership and governance structures. In particular, the voting rule of one person, one vote may constrain the expansion of the financial flows of the cooperative, because it promotes *free riding* by members and causes difficulties in exercising adequate *internal control*, particularly as the organization gets larger (Chaves, 1994). That is, members are discouraged from keeping a large sum of money deposited with the cooperative, because they cannot exercise a degree of control commensurate with the size of their investment and their stake at risk.

Moreover, when external funds are mobilized, there are strong incentives for the credit union to become borrower-dominated, and the conflicts of interests resulting from the dual role of owners and clients may lead to distorted pricing (interest-rate) policies and to insufficient vigor in collecting loans. It has been argued, therefore, that efforts to increase the role of net depositors, coupled with

independent prudential supervision, may help address some of these shortcomings of organizational design (Poyo, 1989; Poyo, Gonzalez-Vega and Aguilera-Alfred, 1993).

Mobilizing deposits, however, is not an easy task (Schmidt and Zeiting, 1998). There is debate about the costs of this task of financial intermediation and about the appropriate regulatory framework required (GTZ, 1997). These challenges are further complicated by the volatility of financial flows in poor, risky environments such as those in West Africa. The purpose of this case study is to explore these issues for the three types of mutualist organizations analyzed.

C. Main Empirical Questions

Several potential lessons for institutional design and paths to sustainability can be learned from the analysis of these three types of mutualist organizations in West Africa. The main questions addressed in deriving these lessons are:

- (a) How have the savings-deposit and credit instruments of these organizations achieved significant *outreach*? How does the breadth and depth of outreach (numbers and levels of poverty of the clientele) compare across these organizational types and how can one describe the market niches where they operate? What explains the degree of outreach achieved?
- (b) How have the loan and deposit instruments of these organizations been adapted to meet the demand for financial services of low-income rural people, especially women, to engage in consumption-smoothing and output-expansion strategies in a highly seasonal and risky environment? Special attention must be devoted to a comparison of deposit instruments (contractual, forced, voluntary) and their adjustment to the demands for reserve holding and liquidity management of the clienteles in this market niche.
- (c) How have the financial *technologies* of these organizations and their use of existing village arrangements facilitated the solution of information and contract enforcement problems in lending in low-income village societies? How sustainable are these village-based arrangements as structural change takes place in these societies?
- (d) What levels of financial *sustainability* are being achieved by these organizations and what explains differences in their success in this endeavor? What types of challenges must be overcome to achieve sustainability in this market niche?
- (e) How have the *ownership* and *governance* structures of these organizations been established at both the first-tier and second-tier levels and how have these structures facilitated:
 - (i) cost-effective savings-deposit mobilization,
 - (ii) protection of depositors in the absence of an external prudential regulatory framework,
 - (iii) a high loan recovery record, and
 - (iv) effective management of outside funds.

- (f) What have been the role and the style of the external technical assistance provided to these systems? What provisions are being made to leave a sustainable central support when the outside organizations leave?

D. Selection of the Organizations

The organizations considered for this case study were selected because they reflect new microfinance mechanisms commonly found in West African countries. Some of the specific organizations were chosen to build upon earlier research on their performance. A description of each program selected is provided in the following chapters.

The choice of an example of the CIDR-sponsored *caisse villageoises* was directed to the *Pays Dogon* in Mali, where this program has achieved its greatest level of maturity. The credit union movement in Niger was selected since it highlights the new kind of WOCCU-type cooperatives that are attempting to innovate and adapt to their local environments. The choice of village banking programs focused on initiatives sponsored by CRS, Freedom from Hunger, and Save the Children because they have each introduced important innovations to the FINCA village banking model to adapt it to an African environment and to address shortcomings of the original model. Several of these innovations have been adopted by the programs in Benin and Mali chosen for this case study.

E. Data and Methodology

The information reported in this case study comes in part from materials collected during earlier West African research at OSU as well as through recent documents from sponsoring organizations such as CIDR and WOCCU. Interviews and documents collected during recent field visits also provided information on these programs.⁶ Field trips were taken in November and December 1997 to Benin and Mali, to assess the current status, organizational structure, and the lending technologies that generate outreach for the *caisses villageoises* and for several US-based-NGO village banking programs.

The visit to the *caisses villageoises* of the Pays Dogon in Mali focused on gathering information on the role and activities of the technical unit (*Service Commun*) and the regional associations by interviewing staff members and elected officials at the headquarters in the town of Koro. Several *caisses villageoises* were visited to gain insight into the role of the members of management committees as well as the extent of villager participation in the operations and control of the *caisses villageoises*. This trip gathered information to complement what was already available from a previous impact study undertaken by OSU (Ouattara *et al.*, 1997).

⁶ These field trips were taken in late 1997 by Korotoumou Ouattara, then Research Specialist with the Rural Finance Program at the Ohio State University, who already had ample experience in the region. This revised version has not updated the information, which represents the situation of the organizations at the time of the visits.

Three village banking programs were visited, one in Benin and two in Mali. In Benin, the field work focused on the CRS village banking activities implemented through several local NGOs. After meeting with CRS staff in Cotonou, to get an overview of the programs, three partner NGOs (CREDESA, GRAPAD, and CERIDAA) were also visited in Benin.

CREDESA operates 24 village banks, GRAPAD operates 19 village banks, and CERIDAA operates 24 village banks, of which 16 are CRS-sponsored. While visiting the local NGOs, meetings were held with the management to learn more about the organization and operations of the NGO, its mission, and principal activities, including the village banking program and all its components. Discussions centered on the role of the NGOs vis-à-vis the village banks, the nature of their assistance and supervision, their savings, deposit and loan policies, as well as the technical assistance received from CRS. Several village banks were subsequently visited to talk to the members and gain their insights, assess the level of their involvement in management, and find out how the members implement the concept of joint liability in their financial activities.

The two village banking programs visited in Southern Mali were associated with Freedom from Hunger in Koutiala and Save the Children in Kolondieba. Freedom from Hunger operates its village banking program in collaboration with the Kafo Jiginew credit union network, whose staff were interviewed both about the program and their regular credit union activities. Subsequently, several village banking groups or associations, as they are called in this program, were visited to obtain additional information regarding the members' involvement and aspirations.

Save the Children operates its program under the name of Group Guarantee Lending and Savings (GGLS). Discussions with staff members at CRS in Kolondieba revealed that some GGLS units were also members of a network of embryonic credit unions in those places where a local credit union already existed while other GGLS units were not. Several credit unions with GGLS membership were visited as well as stand-alone GGLS units. Discussions with members allowed the researcher to learn how the groups had been organized and were run and about plans for future expansion.

All the organizations were remarkably generous with their time and cooperation. The staff kindly provided logistical support when needed, arranged interviews with partners and members, and made existing documentation available.

F. Contents

In addition to this introduction, the document contains six chapters. Chapter II briefly describes the environment in which these organizations operate. Chapter III analyzes key issues related to the performance of some examples of these three types of mutualist organizations. These issues include the nature of their financial technologies, strategies for deposit mobilization, outreach, sustainability, governance arrangements, and linkages to organizational structures. Lessons learnt from this comparative analysis are highlighted. Chapter IV describes the *caisses villageoises* program in the Dogon region of Mali. Chapter V is devoted to the Niger credit union program, and Chapter VI describes village banking programs developed by US-based NGOs in Benin and Mali. Some policy recommendations and a review of outstanding issues are offered.

II

THE ENVIRONMENT

All the organizations visited for this case study operate in West Africa, an environment where low incomes and high risks are the norm. Although the obstacles to the expansion of microfinance in these environments are formidable, West Africa has been rapidly becoming an important laboratory for microfinance experiments.

This expansion of microfinance in West Africa has followed the widespread failure of development finance institutions and state-owned commercial banks along with the first generation of World Bank-sponsored micro and small enterprise finance projects in the 1980s. Only private (mostly foreign) commercial banks remain in operation in the formal financial system and, with the exception of mobilizing some small urban deposits, these banks ignore microfinance, particularly in the rural areas. Mutualist organizations are among the most important new actors in this market niche.

Three new types of microfinance initiatives currently attempt to reach the poor in these countries:

- (a) Grameen-Bank replications and other group-loan programs, including Sahel Action in Burkina Faso. These efforts are not discussed in this case study.⁷
- (b) Mutualist initiatives that emphasize loans to individuals. These initiatives are apparently more successful than those employing group lending technologies, such as the Grameen Bank replications, but they have received much less attention. They represent an institutional alternative both to commercial banks and to financial NGOs. They emphasize deposits along with loan services and rely on individual rather than the group lending technologies based on joint liability. They include organizations such as the *caisses villageoises* and the credit unions.
- (c) Village banking systems that have adapted FINCA-style lending technologies and that have introduced major additional innovations to the original model. Several of these programs are sponsored by US-based NGOs such as Catholic Relief Services, Freedom from Hunger, and Save the Children. They combine some features of (a) and (b), and in some cases they have linked their activities to credit unions.

This case study contrasts traditional mutualist organizations with the better-known village banking systems sponsored by US-based NGOs, in an effort to derive lessons for the sustainability of village banking in general.

⁷ For a detailed discussion see Paxton (1997) and Nguyen (1998).

Table 1. Socioeconomic and Financial Market Indicators for Benin, Mali, and Niger for Selected Years in the Past Decade.

	Benin	Mali	Niger
GNP per capita in 1996 (US\$)	370	250	220
GDP per capita in 1996 (US\$)	418	240	222
Real GDP rate of growth in 1996 (%)	5.5	4.0	3.6
Average inflation rate for 1990-96 (%)	9.7	5.8	6.5
Bank discount rate in 1996 (%)	6.5	6.5	6.5
Money market rate in 1996 (%)	11.4	11.4	11.4
Deposit interest rate for 1992 (%) ^a	7.8	7.8	7.8
Lending interest rate for 1992 (%) ^b	16.8	16.8	16.8
Exchange rate of the CFAF in 1996 ^b	511.5	511.5	511.5
Socioeconomic indicators in 1996:			
Population (million)	5.6	10.8	9.2
Population density (per square mile)	4.4	8.0	7.0
Rural population (%)	69	73	83
Rural dependency ratio ^c	51	51	n.a.
Rural population in absolute poverty during 1980-90 (%)	65	60	35
Urban population in absolute poverty during 1980-90 (%)	n.a.	27	n.a.
Adult female literacy (%)	19	17	5
Adult male literacy rate (%)	42	32	18
Life expectancy at birth for 1990-95 (years)	47.6	46.0	46.5

Source: IMF Statistics and World Resources

- Notes: *a*: The latest statistics available from the IMF were for 1992. There is usually a 4-5 percentage point spread between the discount rate and both the deposit and the lending rates.
- b*: Official exchange rate of the CFAF, which is pegged to the French Franc, in US dollars. Beginning on January 12, 1994, the CFA Franc (CFAF) was devalued to CFAF 100 per French Franc from CFAF 50 at which it had been fixed since 1948.
- c*: Dependent population, ages over 15 and less than 65, as a percentage of the potential labor force, ages 15 to 65.
- n.a. not available.

A. Socioeconomic Features

The organizations selected for this case study operate in one of three West African countries, namely Benin, Mali, and Niger. These three countries share much in common besides their geographic location (Table 1):

- (a) These countries are among the poorest in the world, as reflected by a GNP per capita between US\$220 and US\$370.
- (b) These countries have rapidly growing populations, at rates averaging 3 percent per year, while rates of real GDP growth remain at less than 6 percent per year. Poverty is widespread.
- (c) Population density is low, ranging from 4 people per square mile in Benin to 7 in Niger and 8 in Mali. This low density of population increases the costs of microfinance organizations.
- (d) The rural population in these countries exceeds 70 percent of their total population. Among the rural population, between 35 and 65 percent live in absolute poverty. This rural population faces numerous sources of uncertainty and risk in a fragile environment. Coping with risk and consumption smoothing are at the core of their economic activities.
- (e) Levels of education are low. The adult literacy rate is low, ranging between 18 and 42 percent for males and even lower (5 to 19 percent) for women. Low levels of education also constraint the emergence of formal financial contracts.
- (f) Inflation has not been a problem in these countries, which are all under structural adjustment programs. Thus, between 1990 and 1996, the average inflation rate was less than 10 percent per year. This low inflation rate can be attributed to the strict monetary rules that these countries follow under the West African Monetary Union (UEMOA).

B. Financial Markets

Financial markets in these three countries are characterized by the limited outreach of the commercial banking system, which operates with a high urban bias. Banks are located in the capital city, with just a few or no branches at all in the rural areas. Thus, rural people (over 60 percent of the population) have limited or no access to formal financial services.

1. Mali

The financial system of Mali is still rudimentary, even by African standards. For 1995, the conventional financial deepening indicator (M2/GDP) was only 22 percent compared to other West African countries for which this indicator ranged from 18 to 30 percent. There are a few commercial banks, including the Bank of Africa and the *Banque Malienne pour le Commerce et le Développement* (BMCD). Development banks include the *Banque de Développement du Mali* (BDM) and the *Banque Nationale de Développement Agricole* (BNDA). All commercial banks have few or no

branches in the rural areas. Only the BNDA maintains some business relationships with other semi-formal organizations (such as the *caisses villageoises*) located in the rural areas.

The semi-formal finance world of Mali is dominated by microfinance organizations. The oldest of these organizations were created in 1986, including the *caisses villageoises* in the Dogon region and the Kafo Jiginew credit union network. In 1996, there were 24 registered microfinance organizations with 160,000 members, CFAF 5 billion (US\$ 10 million) in mobilized deposits and CFAF 5.8 billion (US\$ 11.4 million) in loans, of which CFAF 2.1 billion (US\$ 4.2 million) came from the banking sector. These microfinance organizations were able to reach only 3 percent of the working population in Mali (Chao-Béroff and Ellsasser, 1997).

2. Niger

The formal financial sector of Niger has a history of failures of financial institutions one after the other. In 1990, the *Banque de Développement de la République du Niger* (BDRN) collapsed, followed by the *Crédit du Niger* (CN) and the agricultural bank, the *Caisse Nationale du Crédit Agricole* (CNCA). The Nigeria International Bank (NIB) had closed its Maradi office in 1987. Three commercial banks failed between 1988 and 1992: the *Banque Internationale pour le Commerce et l'Industrie du Niger* (BICI-N), the *Banque de Crédit et de Commerce* (BCC), a subsidiary of the infamous Bank of Credit and Commerce International (BCCI), and the *Banque Islamique du Niger* (BIN), which closed in February 1992.

Today, existing commercial banks in Niger have a strong urban bias. They are all located in Niamey, the capital, and they have just a few or no branches in rural areas. The involvements of commercial banks with the agricultural world remains very limited. In fact, financial deepening indicators for Niger are the lowest among Francophone African countries. The only financial system that serves the rural sector via branches throughout the country is the credit union network sponsored by WOCCU, jointly with a few other donor-funded programs.

3. Benin

In 1990, the financial market of Benin underwent a complete restructuring, shortly after the country abandoned its Marxist-Leninist ideology. The restructuring of Benin's state-owned banking sector gave rise to a formal financial sector of five private commercial banks. These are the *Banque Internationale du Bénin* (owned by a syndicate of four Nigerian banks), Ecobank, Bank of Africa, Financial Bank (Lebanese and Swiss owned), and *Crédit Lyonnais* (French ownership). These banks all operate in major urban areas and have few or no branches in rural areas. The national savings bank and postal checking service have wider outreach but offer limited deposit and loan services.

When the *Banque Béninoise pour le Développement* and the *Caisse Nationale de Crédit Agricole* (CNCA), which had been set up to disburse long-term and agricultural loans, were liquidated in 1990, the government withdrew from the management of financial intermediaries and replaced the old system with credit unions or *caisses locales de crédit agricole mutuel* (CLCAM). By December 1997, over 200,000 people were members of a credit union network made up of a federation called FECECAM (*Fédération des Caisses d'Epargne et de Crédit Mutuel*) and 82

CLCAMs operating all over the country. This made FECECAM the largest credit union network in Francophone Africa.

In summary, after a major crisis in Benin, there is now renewed faith in the financial system in general and there are increasingly active semi-formal and informal financial markets. The semi-formal system is dominated by credit unions and other mutualist financial organizations, eager to fill the gap left by commercial banks not able or not willing to serve the rural population and the poor in general. Other players in the microfinance world, such as international projects and programs as well as NGOs, are also trying to share a market of at least 60 percent of the population.

The informal financial sector remains the province of *tontines* and moneykeepers and moneylenders throughout these countries. Unfortunately, most NGOs show a crucial lack of expertise and capacity to engage in successful financial intermediation. All these factors explain the importance of the challenge facing microfinance organizations that choose to work with the poor in the rural areas. Despite these obstacles, mutualist organizations have managed to achieve some success, reaching the poor while remaining sustainable.⁸

C. The PARMEC Law

The countries covered by this study are members of the Franc Zone and of the West African Monetary Union, the *Union Economique et Monétaire Ouest Africaine* (UEMOA). This group includes seven francophone countries: Benin, Burkina Faso, Côte d'Ivoire, Niger, Senegal, and Togo, all of which use the CFA franc (CFAF) as their currency. The CFA franc is pegged to the French Franc (FF), with a fixed parity rate of 100 CFAF per 1 FF, following the devaluation of the currency in January 1994.⁹

The Union was created in 1962 and includes a regional Central Bank, the *Banque Centrale des Etats de l'Afrique de l'Ouest* (BCEAO), located in Dakar, Senegal, with national branches in member states. Monetary policy, interest rates, currency and trading regulations in these UEMOA countries are controlled and determined by the country's membership in the Franc Zone. Exchange controls apply to all currencies other than the CFA franc and French franc. This situation makes it imperative to discuss this regulatory environment since the mutualist organizations studied here are subject to this regime.

Approved as early as 1994 by some countries, including Mali, a new law regulating mutualist organizations was enacted by the BCEAO. The PARMEC law has been intended to provide a legal

⁸ Given great difficulties in defining and in measuring sustainability, this report uses the term *sustainability* in a broad and lax sense. Most of the organizations observed would not pass rigorous tests of sustainability but they have, so far, shown a better performance than their predecessors.

⁹ Since 1948, the CFA Franc was pegged to the French Franc for 26 years at FF 1 = FCFA 50, before the devaluation of 1994.

framework for *mutualist* organizations and savings and credit cooperatives including their unions and federations. The PARMEC law does not apply to *tontines* or other informal savings groups, but these groups are free to apply for recognition under the law. Other microfinance organizations that are not of a mutualist or cooperative type are not subject to the law. These types of organizations will be regulated under each country's separate banking laws.

Mutualist organizations under the PARMEC law must meet the following criteria:

- (a) membership must be free and voluntary,
- (b) membership size is not limited,
- (c) a democratic structure must prevail, following the one-person, one-vote principle,
- (d) short-term assets must at all times be at least 80 percent of short-term liabilities,
- (e) the loan portfolio must not exceed twice the total amount of members' deposits,
- (f) a loan to a single member must not exceed 10 percent of the value of all members' deposits,
- (g) loans to board members cannot exceed 20 percent of the value of all members' deposits,
- (h) portfolio at risk must not exceed 5 percent of the total loan portfolio, and
- (i) at least 15 percent of the annual operating surplus must be kept as a reserve.

Under the PARMEC law, mutualist organizations have their name protected and benefit from tax exemptions. The organizations, however, are also subject to a more restrictive usury law. This law establishes interest rate ceilings on credit. At the end of 1997 it was still unclear whether this ceiling or cap would be equal to twice the discount rate or set according to some other formula. In 1996 this formula would have allowed the organizations to charge up to 30 percent nominal annual interest rates on loans. The usury rate was lowered to 27 percent in 1997. At this rate, not many microfinance organizations would have been able to cover their costs. Final details were still being worked out.

It is worth noting that the PARMEC law was drafted with funding from the Canadian International Development Agency (CIDA), with the technical assistance of *Développement International Desjardins* (DID), the leading Canadian credit union organization. It is not surprising, therefore, that the law emulates features that are prominent in credit unions and credit cooperatives in general. Although the PARMEC law may fit mutualist organizations, it should be recognized that it remains silent on the regulation of other forms of microfinance organizations. In this connection, each country has been left free to set its own laws or no law at all for non-mutualist organizations.

This omission is not a cause for serious concern, however, while the potentially repressive features of the PARMEC law are. While a *prudential* regulation and supervision framework is recommended for deposit-taking organizations, the urge to regulate all microfinance organizations without a clear understanding of the effects of regulation may lead to counter-productive results (Gonzalez-Vega, 1998c).

D. Assessment

In summary, the mutualist microfinance organizations reviewed in this case study operate in a difficult environment. While widespread poverty in these West African countries creates unsatisfied demands for financial services, all transactions are very small. The small size of the transactions and the inadequate physical and institutional infrastructures increase transaction costs for all market participants. Moreover, seasonal patterns, uncertainty, and high risks further conspire against the emergence of insurance and financial markets. It is not surprising, therefore, that formal financial markets are shallow and that they lack particularly in rural depth. While price stability helps, the recent rigid and potentially repressive norms of the PARMEC law, not matter how well-intended, will not contribute much to rural financial deepening. The most promising initiatives are, instead, the innovations and hard work in the field displayed by the organizations discussed in this report and their efforts to incorporate features of informal institutions in their financial technologies and organizational design.

III

KEY ISSUES AND LESSONS FOR VILLAGE BANKS

This comparative analysis of client-owned microfinance organizations in West Africa has identified a number of key issues. Analysis of these issues can lead to lessons for village banking programs in West Africa, as they evolve into larger-scale, fully-functional and sustainable financial intermediaries. Five key issues of general interest are:

- (a) the appropriateness of their financial technologies;
- (b) their strategies for deposit mobilization;
- (c) the degree of outreach and sustainability of these organizations;
- (d) their property rights and governance structures; and
- (e) their linkages and leveraging.

A. Financial Technology

Lending technologies refer to the actions, tools and procedures used by microfinance organizations to reduce expected losses from default and to accomplish this at a reasonable cost (Gonzalez-Vega, 1998b). These tasks involve screening applicants, designing contracts and choosing terms and conditions for different classes of clients, monitoring borrowers, signaling the seriousness of the organization, and enforcing contracts.

All of these mutualist organizations rely heavily on their *proximity* to the clientele to screen and monitor borrowers and on combinations of formal and informal mechanisms to enforce their contracts. The differences in their lending technologies described below have implications for the breadth, depth, and quality of their *outreach*, namely for their ability to offer valuable services to large number of their target clienteles.

1. Individual versus group loans

The *caisses villageoises* and West African credit unions use a *lending technology* mostly based on individual loans, whereas the village banks use some form of group lending. What this means is that, although village bank members may receive either individual or group loans, these are guaranteed by some form of *joint liability*, while this is not the case in the other organizational types. Granting loans to individuals means that the *caisses villageoises* and the credit unions have to rely on physical assets and other forms of collateral for contract enforcement, while the village banks rely on group liability and peer monitoring for loan repayment. This may raise issues about differences in *depth* of outreach (Gonzalez-Vega, 1998c).

The *caisses villageoises*, using an individual-loan technology, ask for physical collateral such as tools and equipment, animals, jewelry, and expensive clothing items for women. This is not a major barrier, however, as most residents of the village possess some of these assets, but the value

of these assets does constrain the size of the loans granted. Indeed, collateral has to be adapted to the local environment, and the assets pledged must represent something the borrower highly values.

Moreover, borrowers who belong to a different village are subject to more stringent rules than residents of the village where the *caisse villageoise* operates, whereby a guarantor is required in addition to physical collateral. The guarantor has to be a member of the *caisse* and live in the village where the *caisse* is located. In this fashion, the managers of the *caisse* are protected because in this fashion they enlist additional screening and monitoring agents, by adding another layer of control through a person whom they know well and to whom they have easy access.

Village groups can deposit funds at the *caisses villageoises* but they cannot be granted loans. Village institutions, such as indigenous village groups and village chiefs play, however, an important role in tasks such as acquiring and sharing information on potential borrowers and facilitating contract enforcement on behalf of the *caisse*.

Credit unions in Niger largely use an individual-loan technology. Nevertheless, some credit unions such as those belonging to FECECAM in Benin and the Kafo Jiginew in Mali provide loans to members of groups. All of these organizations require a variety of collateral, which includes pledges of land and physical assets such as tools and implements, a third-party guarantor, or the group's joint liability.

Village banking programs in West Africa use some variation of a group lending technology. Groups are formed by people, usually women, who live in the same village or town. Since it is difficult for members of large groups of 30-60 women to be intimately connected, solidarity groups of six people on average are typically formed within each village bank. These six individuals know each other well and can monitor each other easily. Group liability is used as a collateral substitute and as a mechanism for contract enforcement. Loan monitoring is, therefore, performed by members of the group, who use peer pressure for loan repayment and who can exclude members who default on their loan from the group, as is the case for the programs visited in Mali and Benin.

Both the individual and group loan technologies have proven effective in ensuring comparatively high repayment rates of more than 95 percent of amounts due. Some village banks have realized, however, that smaller groups of six people who know each other well are better for monitoring purposes than large groups of 30-60 people. This is an important innovation over the original village banking model, which was applied to individuals within the village bank.

Village banking practitioners like the group lending technology because it allows poorer people with no physical collateral to get a loan. As village bank members develop a relationship with the organization and acquire more assets through a number of loan cycles, however, they may value the opportunity to gain access to individual loans against traditional forms of collateral, as is practiced by the *caisses villageoises*. Although this innovation has not been adopted by the village banking programs visited, if it were feasible it may represent an interesting albeit challenging next step for these organizations. Joint liability may still be a cost-effective mechanism to grant very small loans.

2. Flexible versus fixed loan terms and conditions

There are notable differences in the terms and conditions of the loans granted across these organizations. These terms and conditions and their adaptation to actual client demands determine the quality of the services offered.

Loan products are particularly attractive at the *caisses villageoises*. These organizations do not link savings-deposits to loans and do not target loans to particular uses. They provide small loans to rural households at positive real rates of interest. There is not a uniform interest rate structure across these organizations and the rates can be changed during general village assemblies. The *caisses villageoises* do not have an explicit loan size criterion either. The value of collateral determines whether borrowers get the amount they request. There is a general understanding, however, that a single loan amount to any individual should not exceed 10 percent of the total loan portfolio.

Terms to maturity of most loans at the *caisses villageoises* do not exceed one year and loan sizes are rather small, averaging US\$ 99 in 1996. This was equivalent to 40 percent of GDP per capita in Mali. The average term to maturity is six months, and repayments are due as a balloon payment at the end of the loan cycle for farmers whose income flows are irregular and very seasonal. Terms are shorter and loan repayments more regular (weekly or monthly) for traders. Thus, these organizations respond with diverse products to the diverse demands for financial services from their clientele. This responsiveness is valuable, given the features of the environment.

In credit unions, access to a loan is tied to the individual's savings, although the loan-to-savings ratios differ from one credit union to another. The lower the loan-to-savings coefficient, the higher the implicit effective interest rate charged. Loan sizes averaged US\$ 190 in Niger in 1996, equivalent to 73 percent of GDP per capita in that country. Terms to maturity depend on the loan products offered. Repayment schedules include installments as well as balloon payments. Short-term loans average six months, while equipment loans carry longer terms, averaging two years. Such long terms are not offered by the other types of microfinance organizations. Although interest rates are positive in real terms, they vary across credit unions and even within each one of the networks operating in Niger. Interest rates cannot be changed unilaterally by individual credit unions.

In village banks, there is typically a formal limit on the size of the loans, which introduces some rigidity. Loan cycles usually last 16 weeks, with equal installments paid weekly, bi-weekly, or monthly. Thus, terms to maturity are also inflexible. Village bank practitioners believe in instigating a regular repayment habit in their borrowers to avoid default. These payments occur at regular meetings, where the whole membership becomes a witness to the transaction and where peer pressure is exercised.

These programs do not encourage loans for agriculture, which require a longer gestation period and depend on seasonal income flows. Loans are targeted instead to microenterprise activities (mostly trading), which generate regular cash flows, compatible with the program's repayment schedule. Interest rates are positive in real terms and meant to promote operational self-sufficiency. They are set by the implementing agency and cannot be changed unilaterally. The members sometimes freely set, however, the interest rates to be charged on loans from the *internal account* of the village bank.

One challenge for village banks may be that by setting a maximum loan amount for its members, they may induce some, *e.g.*, its older members, to quit the organization when they reach the ceiling. If village banks want to transform themselves into sustainable organizations, they must adapt to the growing demands and wealth of their membership, provided they can secure the larger loans with acceptable collateral. It is not clear if these revisions are compatible with the overall village banking technology and with efforts to keep costs low.

The *caisses villageoises* and the credit unions do not target their loans to specific uses and are thereby able to address the demands of a broader clientele, including farmers. Given the fungibility of funds and the multiple occupations of West African households, it is difficult to identify the actual use of borrowed funds. It is possible, therefore, that funds from all of these organizations are being used in farming, given the importance of this occupation in these countries. Contract terms that are adjusted to agricultural occupations make the loans riskier for the lender but valued by the clients.

3. Mechanisms to collect information and ensure contract enforcement

One attribute of member-owned, village-based organizations is that they possess a comparative advantage over remote commercial banks in collecting information about the borrowers. This advantage comes from the fact that they are located in the same place where their borrowers live and work; *i.e.*, they operate in villages that are fairly small (400 adults on average) and where family and social ties are strong.

In these villages, people know each other well and information is readily accessible and verifiable using family members, friends, neighbors, and members of the same indigenous group as the borrower. This information advantage lowers the costs of screening and monitoring borrowers. When the organization extends its operations beyond the boundaries of a single village or is located in a larger town, these information economies decline and lending strategies must change. Thus, for example, for borrowers who do not live in the village, the *caisses villageoises* require that they provide a guarantor who is a local resident.

One important element in the financial technology of the *caisses villageoises* is the explicit use of village arrangements to facilitate the solution of information and contract enforcement problems. Village institutions, such as indigenous groups and the village chief, play an important role in several aspects of the operations of the *caisses villageoises*. Indigenous village groups are organized along gender and/or age lines. These groups engage in income-earning activities such as the construction of houses and granaries for a fee and the planting and harvesting of a common field. The proceeds from these activities are usually kept at the group level and used to make loans to members. These funds are frequently deposited at the *caisse villageoise*.

First, the village chief is always consulted before the office for the *caisse* it built, and later on he serves as a contract-enforcement resource. This is part of the chief's traditional role in conflict resolution within the village. Second, indigenous village groups that are members of the *caisse* are also enlisted to monitor their members on behalf of the *caisse*. Indigenous village groups have an incentive to monitor individual *caisse* borrowers because they deposit large amounts of money with the organization (Ouattara *et al.*, 1997).

Management committee members are chosen by all villagers in an open assembly. The men and women who are selected to run the organization are trustworthy people who have demonstrated some leadership skills. They also know that they will be subject to village-wide scrutiny. In the *caisses villageoises*, therefore, contract enforcement is obtained not only through the use of collateral but also through village-wide monitoring of the borrowers and by resorting to the authority of the chief if necessary. These mechanisms have so far been effective in keeping default at low levels.

The credit unions and village banks also incorporate village-level information in their decisions and also possess contract-enforcement advantages over other formal intermediaries. Thus, some credit unions, such as the Kafo Jiginew in Mali, use market groups to screen potential borrowers and some village banks use ROSCAs to form their groups.¹⁰ The use of these established informal groups in village banking is not systematic, however, and although market groups are commonly used in Mali, credit unions in Niger do not rely on village groups to screen their borrowers. In the village banks, nevertheless, members of the group (rather than the community at large) are expected to offer peer screening and monitoring. When joint liability is enforced, group members have a strong incentive to be diligent in this task.

Thus, at the *caisses villageoises*, borrower monitoring is performed both by the management committee members and by all villagers. At the credit unions, monitoring is the responsibility of the loan managers. In village banks, loan monitoring relies on group members, who use peer pressure for loan repayment and who can exclude a member who defaults on her loan. The *caisses villageoises* have an easier time monitoring their loans, because the whole village is involved and because loans are backed by tangible assets pledged as collateral. This advantage cannot be exercised, however, in larger urban settings. Village banking programs, in turn, find it more effective to monitor loans through smaller groups of people who know each other well, such as solidarity groups. This is a substitute for physical assets pledged as collateral.

At the *caisses villageoises*, loan default is handled by seizing the borrower's collateral after all other means of contract enforcement have failed. This frequently relies on involving family members and is carried out with the agreement of the village chief. The formal judicial system is rarely used because it would not be practical. In contrast, the credit unions do rely more on the legal system and on group pressure when needed to deal with loan default. With village banking programs, any loan default results in all members of the organization being penalized by loss of access to additional funds. Thus, village bank members rely on each other to repay loans due, but a defaulter may ultimately be excluded from the village bank and from all access to future loans.

In some programs, village bank members are individually responsible for repayment of their loans. These borrowers are allowed to take only the amount they can afford to repay. If members of the village bank come to the rescue of a defaulter, they expect to be paid back. If defaulters do not have valid reasons for their behavior, they are barred from the group. To this extent, some West

¹⁰ See Chapter VI for a discussion of village banking programs and the Kafo Jiginew credit union network in Mali.

African village banks have incorporated features of individual-loan technologies. Where this is the case, the transition to individual loans backed by collateral should not be too difficult in the future.

In summary, all three types of organization use some informal village institutions to minimize the costs of addressing information problems and improve contract enforcement. The *caisses villageoises* relay on *groupements villageois* (indigenous village groups) for monitoring purposes. Some village banks use ROSCA members to form their groups. The Kafo Jiginew credit unions in Mali use *associations villageoises* (village associations) to recruit the first members of their village banks and rely on the associations as a contract enforcement mechanism. These organizations have realized that village institutions possess a wealth of information that can be used to minimize moral hazard and facilitate contract enforcement. They all have, to some extent, incorporated village informational and contract enforcement elements in their lending technologies.

4. Optimum size of village-based organizations

The optimum size of any organization is determined by the point where the costs of expansion outweigh the benefits of mobilizing more deposits from members who reside outside the village. As these organizations grow and reach more distant clients, however, their information and contract enforcement advantages decline.

The *caisses villageoises* and credit unions usually incorporate several villages into one local organization. This creates monitoring and contract enforcement problems when the borrowers do not reside where the organization is located. Serving only people from the same village would alleviate the costs of gathering information for screening and monitoring, but it would reduce the breadth of outreach of the organization and prevent the exploitation of economies of scale. The solution to this trade-off depends on the nature of the lending technology. These organizations use a technology that relies heavily on local information. This constrains their growth potential. The issue is delicate, because the population excluded from villages where there is no *caisse* tends to be poorer than the population of villages with *caisses*.

Village banks tend to restrict their membership to a maximum of 60 people and have realized that even such a number may be too large for proper loan monitoring. Thus, a solution has been found in forming smaller solidarity groups of six people, who have an easier time monitoring each other, within the larger village bank group. This adjustment to the original village banking model is an important innovation.

B. Deposit Mobilization

1. Forced versus voluntary savings

The *caisses villageoises*, credit unions, and village banks all mobilize savings-deposits from their clients, but in doing so they follow different approaches. While the *caisses villageoises* attract *voluntary* deposits, the credit unions and village banks include *forced* savings in their deposit mobilization practices. The borrowers' savings are thus captured by tying loans to deposits and by requiring a contribution to a guarantee fund, which is a percentage of the loan amount disbursed. This practice in effect raises the effective cost of the loans for the borrowers, as the net amount borrowed is lower than the amount used to compute interest payments.

The *caisses villageoises* have adopted a *savings-first* approach. They receive no endowment of funds to start their lending operations. During the first year of operations, for their loans they have to rely entirely on the mobilization of village savings. These are voluntary deposits. There are no forced savings at the *caisses villageoises*, and loan size is not linked to deposits. These are attractive practices. The use of village savings for intermediation helps to avoid creating the image of hand outs that accompanies the operation of some NGOs. More importantly, it acknowledges that access to *voluntary* deposit facilities represents a genuine service to the clients and contributes to true financial intermediation within the village.

The *caisses villageoises* mobilize voluntary deposits by offering attractive interest rates to savers and by ensuring the quality of services (*i.e.*, safe and confidential accounts). They pay high positive interest rates in real terms (nominal rates reached 40 percent per year when inflation averaged 6 percent from 1990-1996). These rates reflect the high opportunity cost of funds within the village. Attractive remuneration of deposits creates a pool of net depositors, essential in true financial intermediation. In fact, the *caisses villageoises* have been able to attract large depositors, mainly from informal village groups and big traders. The average size of these large deposit accounts was US\$ 275.

Individual deposit accounts are small. For large and small deposits, as of December 1996, the average balance was CFAF 62,500 (US\$ 125). Voluntary deposits funded about two-thirds of the total loan portfolio of the *caisses villageoises*. The rest of the funds came from outside commercial sources such as the BNDA, the agricultural development bank of Mali. In general, the *caisses villageoises* try to match the term structure of their assets and the term structure of their liabilities at the level of the local organization, by matching longer-term deposits (3 -12 months) and disbursing shorter-term loans (1-9 months).

All *caisses villageoises* keep a gross intermediation margin of 18 to 30 percentage points, charging interest rates on loans of 36 to 60 percent per year. Interest rates can vary depending on the intermediation and operating costs of each organization and the costs of borrowing from external sources. This wide margin, compared to commercial banks, allows the *caisses villageoises* to cover all their costs, including the payment of external auditing services, and still remain profitable. These profits are used in ways that create *compatible incentives* for the officers of the organization and for the village at large to diligently engage in monitoring efforts.

The *caisses villageoises* attract depositors by offering them the opportunity to choose among several products to meet their demands. There are two basic types of products:

- (a) demand deposit accounts that earn no interest, and
- (b) term deposit accounts (3-12 months) that pay 18-30 percent annual interest rates.

Term deposit accounts are by far the preferred accounts, and they attract more than two-thirds of the total savings collected (Ouattara *et al.*, 1997). This reflects the fact that economic activities as well as consumption patterns are seasonal in the Dogon region. The differential interest compensation is used to overcome a strong liquidity preference in a risky environment and allow the organization to match its loans with deposits of a longer maturity, thus resolving its liquidity management problems.

The *caisses villageoises* also attract depositors by building a permanent and durable structure. The local office of the *caisse* is sometimes the only village structure with a tin roof. The safe, provided by the French sponsor, is located inside the building and protected by another door. Recently, the *caisses* have been upgrading their offices and reinforcing metal doors and windows, after several of them were broken into and the money stolen. These actions became necessary when the members stopped depositing with the *caisses* that had been burglarized. This suggests that these organizations offer a useful safekeeping service in the village. A demand for this service explains the mobilization of non-interest-bearing deposit accounts, as long as safety is guaranteed. In summary, the *caisses villageoises* offer valuable voluntary deposit facilities to their members with deposit products that are safe, well-remunerated, and adapted to their demands.

Credit unions in Niger encourage voluntary savings-deposits but also practice forced savings, by requiring that a proportion of the loan be deposited as a guarantee. This practice increases the effective cost of the loan. Moreover, the guarantee is not truly a protection against a borrower who intends to default, but it may help the credit union address liquidity crunches. In effect, a borrower with lack of willingness to repay would just take the net proceeds of the loan and leave the credit union. By lowering the net proceeds of the loan, however, this practice raises the effective cost of the funds and makes the loan products less attractive for the clients.

Individual members as well as groups can open a savings account at the local credit union. In addition to passbook savings accounts, since 1996 Niger credit unions have offered their members interest-bearing deposit accounts. Guaranty funds offered as collateral also earn interest. This lowers the impact of this requirement on the effective cost of the funds. Furthermore, members are rewarded at the end of the year when profits are distributed and each member receives a dividend proportional to the amount of savings held.

The interest-bearing deposit accounts introduced in 1996 were an effort by management to encourage savings and especially to attract more women, known to be a potential market of net savers. When an organization relies heavily on deposits for its lending activity, it is essential to find ways to keep a continuous and even increasing flow of deposits to meet loan demand. This creates new attitudes among management.

Village banks in West Africa encourage their members to voluntarily save with their programs, but they also insist on collecting forced-deposits from the members. Voluntary deposit amounts are very small and are usually withdrawn at the end of each cycle. This may reflect the conflicting incentives that emerge when voluntary and forced deposits coexist. In this case, the organization is sending mixed signals. On the one hand, savings are a requirement that makes loans expensive (negative signal); on the other hand, deposit facilities are a valuable service (positive signal). It is difficult to simultaneously promote both. Ultimately, to encourage more *voluntary* deposits and to create a pool of net savers, village banks will have to revise their structure of incentives, including the quality of the services offered to depositors. This is not a trivial challenge and may be beyond the administrative capacity of many village banks.

The contrasts between organizations that practice forced savings versus those that offer voluntary deposits are striking. Organizations such as the *caisses villageoises* and the credit unions, which practice voluntary savings, devise ways and create products and mechanisms to attract depositors. This includes different deposit products at different terms to maturity and attractive interest rates. To gain the respect and confidence of their depositors, these organizations need to meet a minimum set of requirements, such as a good physical structure that can resist theft and fire and other weather-related hazards and reliable safes. Good management of the loan portfolio is essential to attract depositors. If there are voluntary depositors who can withdraw their savings, management will feel constrained and will be more prudent in their lending operations (Poyo, Gonzalez-Vega and Aguilera-Alfred, 1993).

2. External funding

One element that differentiates the *caisses villageoises* and credit unions from the village banks is the extent and nature of their reliance on external funding. The village banks start their program with external funds while the *caisses villageoises* and credit unions emphasize a savings-first approach. That is, in the early years of the organization, they exclusively rely on deposits.

The *caisses villageoises* believe in instigating a savings habit among their members. It is also important to make villagers aware that the organization belongs to them. By the time the *caisses villageoises* gain access to outside funds, in an effort to meet increasing demands for their loans, the members are already convinced that they are working with their own money and that they have to be disciplined in their use of the loan funds. This allows these organizations to increase the supply of funds at the village level without skewing the positive role of depositors.

The external funding approach of the village banks introduces another foreign element to the program in addition to the rules and regulations brought over by the foreign implementing agency. To rely on external funds for on-lending does not encourage savings by program members beyond those required for borrowing. Emphasis, instead, is placed on credit and, in the end, the programs tend to be supply-driven rather than demand-driven. It is true that members are required to accumulate savings, but these funds represent a counterpart contribution to the loan (they are not more than guided *self-financing*); they are not funds *intermediated* from surplus to deficit units in the village. As a result, there is less intermediation of local funds than would be possible otherwise.

Village banking programs do not necessarily have to rely on external funds for on-lending at the beginning of their operations. For example, the Freedom From Hunger (FFH) programs in West Africa work in partnership with credit unions and other microfinance organizations, and FFH does not provide its programs with donor funds to be on-lent to members. This is a better approach than the original village banking model in promoting financial intermediation.

Village banking programs have to realize, as do the *caisses villageoises*, the importance of deposit services for people living in risky environments. Liquid savings with a financial organization are frequently a better and safer alternative for these populations, who currently hold most of their assets in physical forms such as livestock. A drought might easily wipe out these physical assets, while financial assets will survive such negative shocks. In addition, the economic environment in West Africa is very suitable to the mobilization of financial savings, since it is a low inflation environment. Deposits largely maintain their real value from year to year and their liquidity is a valued attribute. Most of these mutualist financial organizations have not yet captured the full savings potential of their clienteles.

The savings-first approach adds strength to the organizations practicing this strategy. Issues concerning the stability of member deposits and the cost-effectiveness of deposit mobilization need, however, to be recognized.

Because the *caisses villageoises* practice a savings-first approach, they are stronger organizations than otherwise, as members and especially depositors have a higher stake in their performance. They want to see the organization succeed and, therefore, they exercise more monitoring over the activities of its managers and the behavior of its borrowers. This improvement in *internal control* and in financial policies as a consequence of a stronger depositor presence has also been observed in credit unions elsewhere (Poyo, 1989).

Monitoring both management and borrower behavior is in the best interest of depositors, who want their investments to be safe and profitable. Management will work to keep deposits and to attract new depositors by offering new and better products or, at least, maintaining the quality of existing products. Offering term deposit accounts, for example, ensures some stability of deposits, essential for the strength of a savings-first organization. Management can also influence the behavior of depositors to reduce the costs of deposit mobilization. Thus, a large number and amount of term deposit accounts relative to current and passbook accounts reduces the costs of mobilizing deposits, because the costs of liquidity management are an important component of these costs and demand deposits pose greater liquidity-management challenges. Hence, cost-effective deposit mobilization depends on the management's willingness and ability to offer and manage deposit products that attract new members, are comparatively stable, and imply low handling costs. While the size of deposits in these organizations is small, which increases average costs, procedures are simple, which lowers costs.

The potential impact of outside funds on the incentives for deposit mobilization should not be neglected. Outside funds can adversely affect deposit mobilization by reducing management incentives to pursue these funds in the local market. To prevent this, some precautions must be

taken. In the *caisses villageoises*, for example, a local organization can have access to BNDA funds only if:

- (a) it has been in operation for at least one year,
- (b) it has high quality management, and
- (c) it has a loan default rate of less than 15 percent of the total portfolio.

In addition, the amount of the BNDA loan to the *caisse villageoise* is a function of the amount of deposits mobilized, *i.e.*, the loan cannot exceed 150 percent of outstanding deposits during the first two years of operation and 200 percent thereafter. These conditions have apparently proven successful in avoiding a negative impact of BNDA funds on deposit mobilization.

In addition, the BNDA funds are not grants but loans at 18 percent annual interest to the *caisses villageoises*, which in turn lends the funds to its members at its regular interest rates of 30 to 60 percent. Thus, for the ultimate borrower, these are not subsidized funds and are not different in price from loans based on deposits. The outside funds do not create, therefore, disincentives to repay. Rather, these outside funds have allowed the *caisses villageoises* to better meet an increasing demand for larger loan amounts and longer terms to maturity, which was not being met through mobilized deposits alone.

A potential lesson from this experience is that village banks may consider engaging in voluntary deposit mobilization from the onset. Voluntary deposits provide strength and discipline to the organization, as depositors become interested in its performance and sustainability. To attract net savers, however, the organization must pay positive interest rates in real terms on deposits. Most important, however, is the safety of the funds, which requires adequate control mechanisms. To be able to offer safe services would be a major challenge for village banks.

In contrast, to start operations exclusively with outside funding does not create sufficient incentives for the early mobilization of voluntary deposits. Outside funds become necessary in poor environments, however, when credit demands grow, but only as a complement and not as a substitute for locally mobilized funds. It appears that these outside funds can be incorporated without distorting incentives when the mobilization of local deposits is already well established.

Village banks do mobilize savings from their members, but the regimented schedule of forced-savings and the linkage of savings to loans reduces the value of the service for the client. Moreover, this mechanism is not adequate to attract a minimum mass of net depositors. Members in village banks currently participate because, given their alternatives, they are interested in the credit products of the village bank, not because they like the savings dimension. Even though a few may take advantage of voluntary deposit opportunities, which have been offered in some village banking programs, the design itself is not conducive to attracting members simply because they like the deposit products, even when they may not be interested in loans. It is these pure depositors, nevertheless, who would become the best monitoring agents of the performance of the organization. They will not be attracted unless valuable deposit services, delinked from credit, are offered. This challenge may not be easy to address by village banking programs, given the rigid link between savings and loans.

The experience of the *caisses villageoises* illustrates, moreover, that access to funds from outside the village is valuable, given highly binding local wealth constraints in a risky environment. As a whole, the village is a deficit unit and will attract funds from outside. The challenge is how to accomplish this without discouraging local deposit mobilization and, thereby, local intermediation. While the village as a whole is a *deficit* unit, some agents (such as some local groups) are *surplus* units and are willing to deposit independently of their demand for loans.

It is not clear, however, if the limited extent to which even the *caisses villageoises* have succeeded in this effort is mostly a reflection of these wealth constraints or of cultural habits at the local level or if access to the BNDA funds has after all introduced some negative incentives for deposit mobilization.

If the necessary precautions are taken, it may be possible to successfully attract outside funds to complement available local deposit funds. For this task, village banks would have to provide some minimum logistical elements usually needed to mobilize deposits, such as a permanent physical infrastructure made of durable and resistant material, a reliable safe, as well as a trustworthy and knowledgeable management committee backed by strong technical assistance from the implementing NGO. Some of these requirements go beyond the simple, standardized, and not-that-formal structures and procedures of village banking. To supply them may increase the costs of reaching these clienteles beyond reasonable levels. Linkages to other financial intermediaries may provide a means for addressing some of these challenges (Ouattara and Gonzalez-Vega, 1998). Only experiments such as those observed in West Africa can elucidate this empirical question.

C. Outreach and Sustainability

1. Outreach

The *caisses villageoises*, credit unions, and village banks aim at reaching *the poor*. Because of their different financial technologies, some of these organizations have been more successful than others in achieving sufficient breadth and depth of outreach.

By December 31, 1996 there were 21,950 members in 52 *caisses villageoises* in the Dogon region of Mali. Some of these organizations reached as many as 95 percent of the adult population of the village where they operate. Management committee members continuously work on the challenge of bringing more members to the organization. One reason for this extensive outreach is the community-oriented focus of the *caisses villageoises*, which allows all villagers to actively participate in the general meetings of the organization. Another reason is the focus of the *caisses villageoises* on savings-deposits, which meet a widespread demand for financial services and which make villagers feel that the organization belongs to them.

These organizations are located in one of the poorest regions of Mali, and their deposit and loan services are meant for poor people in remote rural areas. Female membership at the *caisses villageoises* ranges from 20 to 50 percent. Average loan size in 1996 was US\$ 99, equivalent to 40 percent of the GDP per capita in Mali. These indicators suggest that these organizations are reaching the poor.

Membership in the Niger credit unions grew at a rate of more than 100 percent per year, with more than 10 *caisses populaires d'épargne et crédit* (CPECs) created every year from 1990 to 1994. By December 31, 1996 there were 65 credit unions with 12,340 members, of whom 30 percent were women and less than 2 percent were groups. Thus, the average membership per CPEC was 195 members. About 40 percent of the total number of loans granted went to women. The average loan size was US\$ 190 in 1996, equivalent to 73 percent of GDP per capita in Niger. While these credit unions are reaching a respectable number of people located in poor areas of the country, they are not reaching the poorest of the poor.

Village banking programs aim at reaching the poorest. On average, loan sizes range between US\$ 50 and US\$ 175. These loans are comparable in size with those at the *caisses villageoises*. Because of their gender focus, moreover, village banks reach more women than other programs. The average female membership in the West African village banking programs was 90 percent. If gender matters for depth of outreach, this weights the outreach of village banks favorably.

Compared to the individual *caisses villageoises* and credit unions, a single village bank achieves a smaller breadth of outreach. A village bank does not usually exceed 60 members, compared to 100 to 400 members per *caisse villageoise* or credit union. The outreach of a single bank in a particular village may be limited if the implementing agency desires to create only one bank per village.

The design of a village bank creates diseconomies to the size of the membership, suggesting the desirability of continuing the limits on membership size but eventually allowing more than one to operate in a village. Moreover, when several village banks come together in a single structure such as becoming members of a credit union, they can achieve significant breadth of outreach. In the Freedom From Hunger program in Mali, up to 22 village banks or credit associations, grouping over 300 members, belonged to a single credit union. This design combined the monitoring advantages of low numbers of members per bank with the advantages of a larger network of clients.

2. Sustainability

All of the programs reviewed for this case study claim that they achieve repayment rates of over 90 percent of outstanding loans. This is a better repayment performance than in many other equivalent programs, but it still causes losses from arrears and default. The long-term sustainability of these organizations depends on their ability to keep these losses from default at minimum levels and to not only cover operational costs with revenues generated from their financial activities (operational self-sufficiency) but to cover both operational and financial expenses with their own revenues (financial self-sufficiency).

Operational self-sufficiency, i.e., the ability of the organization to cover its operational costs with its own revenues, was 177 percent at the *caisses villageoises* for 1995 and 1996. At the Niger credit unions, operational self-sufficiency had been steadily improving over the years, to reach 120 percent in 1996. Operational self-sufficiency was more difficult to achieve in the village banking programs, where less than 40 percent of organizational costs were being covered with revenues in

1996 and 1997.¹¹ Moreover, although in 1996 the Niger credit unions were able to obtain a positive net operating margin (financial self-sufficiency), only the *caisses villageoises* demonstrated that they had consistently reached this level of sustainability.

Thus, the *caisses villageoises* and the credit unions have apparently been able to reach higher levels of sustainability than the village banking programs. One reason may be that the latter programs are younger (less than five years). Costs should decline with the age of the program because learning processes and economies of scale are important (Gonzalez-Vega et al., 1997). The former programs may always fare better, however, because they are able to generate substantial revenues from their lending operations, keep their costs down by using local resources, and/or operate in less difficult market niches compared to village banking programs.

The *caisses villageoises* seem to have been able to achieve a better combination of outreach and sustainability outcomes than either the credit unions or the village banks. This may be due to the fact that the CVECAs are well adapted to the circumstances of the village environment and have adopted pricing policies (interest rates) compatible with their sustainability. By using village institutions for management of the organization, loan screening, and borrower monitoring, the *caisses villageoises* are able to keep their operating costs down, thereby achieving financial self-sufficiency without relying on outside subsidies. This, in turn, creates correct signals to potential clients about the organization's expectations with respect to their behavior.

D. Ownership and Governance

A feature common to the *caisses villageoises*, credit unions, and village banks is their client-owned property rights structure. This feature creates ownership and governance deficiencies, and each type of mutualist organization deals with these shortcomings in different ways at different stages of their development.

General assembly meetings at the *caisses villageoises* are attended by the whole village and not by members alone. Members of the *caisses villageoises* believe that the organization belongs to the whole community, and there is an on-going effort to attract the maximum number of villagers to the *caisse*. The performance of the *caisse* is reviewed in these village assemblies, which also determine all loan and savings-deposit policies, including interest rates. These policies can be adjusted in each village with everyone's consent.

¹¹ See Chapters IV, V, and VI for performance indicators for these organizations. These indicators are crude approximations, as the validity of the information provided by the organizations was not independently verified and as appropriate adjustments, including proper identification of operational subsidies and of the opportunity cost of funds, were not made.

In Niger and other West African credit unions, general assembly meetings are attended by members only and are a forum to discuss the results and performance of the organization as well as planning for the future. Meetings are typically well attended. Other incentives provided by the management, such as a lottery during the meeting, may help to boost attendance.

Village bank members meet often and regularly for loan repayments. At these meetings they may conduct other activities such as health and nutrition education (MkNelly, 1997). Only members attend the meetings, and any absence or even tardiness are penalized. The meetings are the place to discuss any problem, frequently related to loan repayment. Changes in the by-laws cannot usually be made without the approval of the implementing agency, *i.e.*, the US-based NGOs.

Unlike the *caisses villageoises*, village banks are handed down a technology that they are not allowed to alter without the consent of the implementing NGO. Some observers feel that general meetings should be a forum to discuss the performance of the organization and to plan for the future in light of past activities. If village bank members express the desire to modify the structure of interest rates, loan sizes, and contract terms, their requests should be given consideration if the program is to be demand-driven and designed to meet the interests of members. Experts on village banking believe, however, that standard terms and conditions are needed to keep costs down and to facilitate control to prevent fraud.

Poorly-specified property rights can threaten the sustainability of any organization. At the *caisses villageoises*, ownership of the organization is widespread and diffused. In general, the villagers acknowledge that the *caisses villageoises* belong to the whole village, and the organizations are managed by the villagers without outside intervention. Management committee members are elected in a general assembly of all villagers, which also includes non-members. Thus, management committee members feel accountable to the whole village. In small, closely-knit settings, this helps prevent opportunistic behavior.

Management committee members are reelected every three years. This gives other villagers the opportunity to manage the *caisse villageoise*, and it provides incentives needed for management to perform well if they wish to be re-elected. Moreover, the members of the management committee earn profit-based remunerations. This type of remuneration creates compatible incentives that promote good performance.

The residual claimant of the assets of the *caisses villageoises*, however, is the community. If a local *caisse* were to be closed or go bankrupt, the remaining assets would be given to the village to be used for community development or would go to another community group designated by the villagers. This mobilizes support, but responsibilities for control of the organization are still diluted. Free-riding is always a threat in these cases.

Thus, the experience of the *caisses villageoises* indicates that elements of design may, up to some point, compensate for the weaknesses of the property rights structure of a *mutualist* organization. First, making management committee members accountable to a large constituency which monitors their behavior may reduce the threats of opportunistic behavior. Because this monitoring is not too costly for villagers who live in close contact, free-riding may not be a major

concern. Second, remuneration of committee members only when profits are earned through interest earnings from loan repayments also creates incentives that are compatible with the long-term sustainability of the organization. Third, a decentralized operation avoids the accumulation of power by managers, which creates conflicts of interest in more centralized operations.

So far, the *caisses villageoises* have thus been successful in addressing the governance threats emerging from this diffused ownership structure. In particular, they have been able to avoid the power struggles so common in credit unions, in part by remaining as decentralized units with no major overarching superstructure. Indeed, the second-level structure of the *caisses villageoises* model is made up of three regional associations. These associations are only coordinating institutions, however, whose primary role is to obtain outside funding on behalf of the *caisses*. The associations do not intermediate funds between deficit and surplus *caisses* and do not interfere with the financial policies of each independent *caisse villageoise*.

The *Service Commun*, at the third level of the *caisses villageoises* system, is a technical-assistance unit whose services are paid for by the *caisses*. It is not a central finance facility. By making the *Service Commun* an independent auditing and technical assistance entity, the *caisses villageoises* have been able to avoid the power struggles that develop when members and technicians are joined in the same organization, such as a credit union federations and other second-level apex organizations (Ouattara and Gonzalez-Vega, 1998). Much care has been taken in the design of the system to avoid these power struggles (Chao-Béroff, 1998)

The village's power structure, level of trust, and other informal elements such as the existence of indigenous village groups have proven important in combating these governance threats at the *caisse villageoise* level. As these mechanisms may disintegrate with the process of structural adjustment, increased social differentiation, and economic growth, the *caisses villageoises* may have to move from an informal to a more formal governance structure. This will not be an easy transition. One likely evolutionary path is to rely more on a prudential regulatory framework to solve ownership and governance issues with external assistance.

The PARMEC law would in principle offer such a framework. This legislation provides the system with regulations for prudent management and allows the organizations to have recourse to the law to resolve problematic issues. Adoption of the PARMEC framework, however, also carries with it one major hurdle, namely an interest rate ceiling on loans. An interest rate that is too low to cover operational costs and lower than what is currently practiced at the *caisses villageoises* would reduce intermediation margins and would pose legitimate threats to their ability to mobilize deposits. It would also greatly reduce the chances for expanding the network of *caisses villageoises*, as the operational costs of newer organizations tend to be higher in these early stages and require, thereby, higher interest rates. There is still hope that the usury law embedded in the PARMEC law can be revised, as it is tested in the field through implementation by microfinance organizations and as its negative implications are more widely recognized.

Another well-known conflict of interests emerges between borrowers and depositors in member-owned organizations. As a result, there is a threat that an organization may become borrower-dominated. When this is the case, borrowers drive the organization with rules that benefit

them, such as lower interest rates on loans, even below sustainable levels, and less stringent collateral and repayment requirements. This situation can be successfully dealt with and avoided if the organization adopts a *savings-first* approach.

A savings-based organization, where voluntary deposits are the primary source of loanable funds, will have less chance of having borrowers dictate rules that may prove detrimental to the sustainability of the organization. When the organization does not link member deposits to their loans, members become acutely aware of the true financial intermediation role played by the organization and of the value added generated. This awareness helps prevent that net borrowers jeopardize the future of the organization. The voting rule of one person, one vote conspires, nevertheless, against the possibility that strategic depositors could exercise a better degree of monitoring of management and internal control of the organization. The lack of ability to exercise sufficient internal control thus discourages important net depositors from placing their funds with the organization.

E. Linkages and Leveraging

1. Linkages

Whatever the role, style, and extent of the technical assistance provided to these organizations, provisions should usually be made to leave a sustainable central support base when the outside sponsoring agency leaves. Exit of the provider of technical assistance should usually happen only after several years.

For the *caisses villageoises*, technical assistance was provided by the CIDR for eleven years. From 1986 to 1995, the CIDR paid for a resident expatriate advisor as well as for Malian personnel hired for the project. The CIDR also covered operating expenses at the project's headquarters located in the region. Other costs of technical assistance included start up funds to buy office furniture and equipment, including safes, for the *caisse villageoises*. There were, however, no funds for on-lending and no pressures to require that loans be subsidized.

Training of management committee members and cashiers was also provided by the CIDR. Regular inspection of the books, the generation of financial statements and of indicators of performance, and annual audits of the *caisses villageoises* were also part of this technical assistance. The external assistance ended in 1997, when the CIDR pulled out and left the *Service Commun* in charge of the task.

The design of the *Service Commun* should ensure its future success. This comes from the fact that this unit charges the *caisses villageoises* for the services rendered, in order to cover its own operating costs. Only profitable *caisses* contribute, however, to the *Service Commun* earnings. It is believed that this would prevent poorly-performing *caisses villageoises* from being burdened further while it would not allow them to escape the monitoring by the system. This arrangement generates, moreover, compatible incentives for the technicians at the *Service Commun*, as profits made by the *caisses* are critical for the sustainability of their own unit and, thereby, their own jobs. The independence of the *Service Commun*, run exclusively by Malian technicians, allows the unit to

offer its services to other organizations in Mali in addition to the *caisses*, which further contributes to its independence and sustainability.

For the Niger credit unions, technical assistance was originally provided by WOCCU. This assistance lasted seven years, and it included expenses related to two resident foreign advisors, operating costs for one headquarters office in the capital city, and two offices in remote parts of country. The technical advisors and trained managers made regular inspections of the credit unions. They also helped with accounting and financial statements as well as with preparation for annual meetings. By the time WOCCU left the program in June 1997, a second-level support facility was being put in place, which would take over the technical assistance function as well as act as a central financing facility. While the central financing facility can play a useful role, there are important dangers from mixing the technical assistance and funding functions (Gonzalez-Vega, 1998a).

All West African village banking programs have a second-level support base provided by the implementing international NGO. External technical assistance is usually not directly offered, however, and assistance has to be provided by either a local NGO (CRS Benin) or a credit union (FFH Mali). This two-layered technical assistance mechanism incorporates training in village banking methodology and financial management for the local NGO. Funds are also provided to cover the operating costs of the local partner and for on-lending to village banks.

In turn, the implementing NGO is expected to maintain a relationship with a village bank that lasts roughly three years, *i.e.*, the time frame required by an individual village bank to go through several loan cycles and presumably become self-sufficient. This frequently does not happen in practice. No matter when the implementing international sponsor decides to leave, village banking practitioners are aware that a local support structure should be in place before the external technical assistance ends. Several village banking programs have chosen diverse institutional options for this link:

- (a) A permanent relationship between the village banks and the implementing international sponsor, which creates subsidiaries in each country for the sole purpose of implementing village banking activities.

The local subsidiary may attempt to transform itself into a regulated financial institution (*e.g.*, FINCA Honduras, World Relief). This is possible when the regulatory framework in the particular country offers a favorable climate for transformed NGOs. This option may have to be considered when there are no microfinance organizations or commercial banks in the country with which the implementing agency can form a partnership. This option may create, however, a dependency on the implementing agency, and it fails to solve the graduation issue.

- (b) A permanent relationship between the village banks and a commercial bank or a credit union, facilitated by the in-country affiliate.

This scenario exists in Mali with Freedom from Hunger (FFH) and Save the Children Foundation (SCF). Clients of village banks are expected to graduate and become clients of the credit union. This option can be quite attractive if viable credit unions or comparable microfinance

organizations exist in the country. When integrated into a viable financial structure, the permanency of the village banking organization is promoted from the onset. The graduation problem is handled by members of the village bank becoming full members of the credit union and being able to demand individual loans.

- (c) A federation of village banks (apex organization) replaces the support functions of the implementing agency and accesses commercial sources of funds.

This scenario is most preferred by CRS, which plans to create apex organizations in Benin and Sénégal. This option for village banking sustainability raises additional questions, given concern with the design of apex organizations. There are serious institutional shortcomings of apex mechanisms (Gonzalez-Vega, 1998a). No apex organization should be considered if there is not a critical minimum mass of partner NGOs and/or village banks in the country that justifies its creation. The apex organization should be concerned with its own sustainability, and the success of the apex organization depends highly on the nature of its assistance. An apex organization that channels donor funds free of charge to partner NGOs cannot create incentive-compatible credit contracts. Additional analysis may be needed to determine the optimal second-tier link for village banks.

2. Leveraging

The linkage of the *caisses villageoises* to the banking sector through the BNDA has been valuable. The BNDA has become an additional party in monitoring the performance of the *caisses*. In turn, being able to leverage their own lending capacity with outside funds has allowed the *caisses villageoises* to stretch their deposit base and sustain their growth. Leveraging the funding structure with commercial funds is thus a valuable organizational feature as well as a sign of soundness of the *caisses*. This is so because the financial viability of the organization must be demonstrated before it becomes eligible for the bank's loans.

The link to the banking sector sought by the *caisses villageoises* is different from the credit unions' goal of transforming their central financing facility into a banking unit, thereby competing with the commercial banks. The *caisses villageoises* are a complement to the formal banking system and attract outside funds to the rural areas to be added to their deposit base. At best, the central financing facility intermediates a given volume of funds among CUs. At worst, it taxes individual credit unions to provide a liquidity management service. This is a useful but expensive service, and overall it does not attract additional funds for the local clientele.

Some village banking programs have been able to take advantage of the leveraging power of partner organizations as in the case of FFH and the Kafo Jiginew in Mali. As with the *caisses villageoises*, the Kafo Jiginew network has been able to attract commercial funds from the BNDA to onlend to its member organizations. A major flaw of the original village banking model was the creation of transitory, not permanent, links of the stand-alone village banks and the financial system. This creates a self-defeating structure of incentives. One possible solution to the permanency problem is to make village banks part of another viable microfinance organization, such as a credit union or even a *caisse villageoise*.

The institutional lessons learned from the *caisses villageoises* tell us that creating a permanent physical structure from the onset is important. This infrastructure from the beginning that a *caisse villageoise* is a serious financial organization, while a village bank looks more like an informal ROSCA. This village bank lacks a physical structure, and its management have undefined powers and authority. Stand-alone village banks may regard the implementing agency as the ultimate owner of the village bank and as the power that dictates all rules and regulations. A framework for ensuring institutional incentives for sustainability and accountability at all of the organizational levels in a village banking program would require that the village banks develop either the links to other intermediaries or a physical and institutional structure to more effectively signal and guarantee their permanence.

Another lesson learned from all of the programs included in the case study is that direct *hands-on technical assistance* is important, particularly in the early years of the program, and that the sponsoring agency should plan to provide comprehensive and fairly long-term assistance. Before this technical assistance ends, a support base should be left in place. This support facility should be able to bring member organizations to a desirable level of sustainability.

Currently, two alternative designs for a central support facility exist in these microfinance networks in Francophone West Africa. In one case, a central support facility engages in purely financial activities. It must have a comparative advantage for this task. This is the case of the central financing facility of a credit union network, which intermediates funds among member credit unions and from outside donors. In the other case, a central support unit engages exclusively in market-driven, user-charge technical assistance services, such as the *Service Commun* of the *caisses villageoises* system. In this case, member organizations turn to the commercial banking sector or other markets for funds. These specialized mechanisms seem to be more successful than apex organizations that combine both financial and technical assistance functions. Both types of specialized central facilities may offer valuable services. It seems important, nevertheless, to keep channels for funds and the provision of technical assistance as separate as possible.

IV

THE *CAISSES VILLAGEOISES* IN MALI

The *caisses villageoises* as a model of microfinance were developed in the mid-1980s by the *Centre International de Développement et de Recherche* (CIDR), a French NGO located in Autrêches, outside Paris. This methodology is thus almost as old as the FINCA village banking model. The *caisses villageoises* were first started in Burkina Faso. They can be found today in several other West African countries including Mali, the Gambia, Niger, Madagascar, Ethiopia, and Sao Tomé et Príncipe (Chao-Béroff, 1997). The Mali program has achieved the highest level of maturity thus far, and it is the focus of this case study.¹²

A. Evolution and Organizational Design

The system of *caisses villageoises d'épargne et de crédit autogérée* (CVECA_s) was established in 1986 in the Dogon region of Mali by the CIDR, with the financial support of the KfW, the German development bank. There were 52 *caisses villageoises* in existence in the Dogon region by the end of 1997. At that time, these organizations offered financial services to 21,950 members. After eleven years of existence, the program achieved its latest institutional step in July of 1997, when the CIDR left the system entirely in the hands of the villagers and of a Malian technical staff.

The CVECA_s system consists of three levels of operations and management:

- (a) the *caisses villageoises*,
- (b) the *regional associations* of CVECA_s, and
- (c) the *Service Commun*.

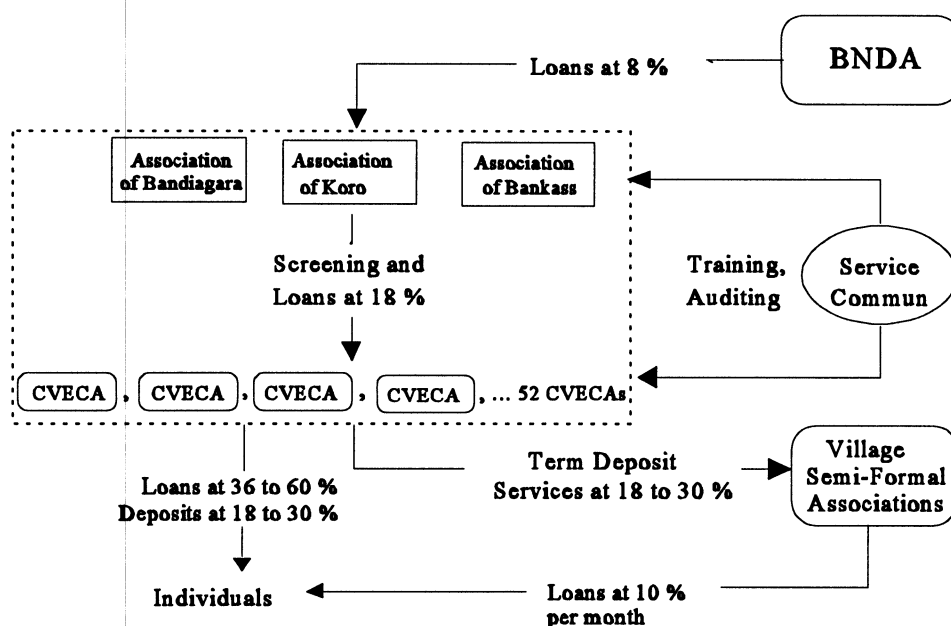
Linkages among these three levels of the system's organizational structure and the terms of the financial transactions at each level are depicted in Figure 1. The interest rate structure that accompanies the flows of funds across this organizational set up is discussed below. Each level has well-defined functions, examined next.

1. The *caisse villageoise*

At the first level of the organizational structure are the local *caisses villageoises*. According to the CIDR, the *caisse villageoise* is "more than merely a bank based in a village." It is a microfinance organization that belongs to the villagers, and it is structured in such a way that it fosters community development. Thus, profits from the intermediation between savings-deposits and loans are invested in community development projects such as school construction, well pumps, and the like.

¹² For a detailed evaluation of the *caisses villageoises* system, see Gonzalez-Vega, Nguyen and Ouattara (1998) and Ouattara, Nguyen, Gonzalez-Vega, and Graham (1997).

Figure 1. Organizational Design at the Caisses Villageoises Model



This allocation of profits to village-wide projects (residual claims) and active village-wide participation in the governance of the *caisse villageoise* are important elements in the structure of incentives for decision-making. These incentives are critical because the *caisses villageoises* are highly independent organizations without well-defined owners. They are designed to operate in a highly decentralized system, in which all but a small portion of the activities required to manage the CVECAs are provided by the villagers themselves. For this participation to be successful, the right structure of incentives is needed.

The creation of a *caisse villageoise* begins with a feasibility study conducted by the CIDR about the village's economic potential, literacy level, history and social cohesion, as well as a potential membership size of more than 400 adults.¹³ This effort to determine the feasibility of a *caisse* in the particular village also determines the *depth* of outreach of the system. Inevitably, poorer and more remote villages are not eligible for a *caisse*.

If the results of the feasibility study are positive, a general assembly of all villagers is called to discuss matters related to:

¹³ This description refers to the first eleven years of operation of the Mali system. After July 1997, the functions formerly performed by the CIDR were completely absorbed by the *Service Commun*.

- (a) the construction of a building to house the *caisse*. The village provides construction materials and labor while the CIDR provides the safe, a metal door, and office equipment. Village inputs contribute to strengthening the sense of village ownership of the organization;
- (b) selection of a Management Committee made up of villagers, men and women, chosen by their peers. Two cashiers and a comptroller are also chosen to work for the *caisse villageoise*. All elected officers are then trained by the CIDR before the opening of the *caisse*; and
- (c) adoption of internal rules and regulations including levels of interest rates and membership fees. Fees are kept low (equivalent to US\$ 1 to US\$ 3) to allow everyone to become a member. Active village participation in the governance of the *caisse* supports monitoring efforts that constrain opportunistic behavior by *caisse* officers and that contribute to contract enforcement.

2. The regional association

A regional *association* represents the second level in the organizational structure of the system. It is a union of all *caisses villageoises* from a particular region. It serves as an umbrella and as a coordinating institution. One of its primary roles is to obtain external funding for the member CVECAs. There are three associations in as many regions where the *caisses villageoises* are located in Mali. The *association's* staff is made up of selected management committee members from the individual *caisses villageoises*.

3. The *Service Commun*

The *Service Commun* represents the third level of the organizational structure. It is a central unit whose role is to provide financial and technical support services to the *associations* and to the *caisses villageoises*. It replaced the expatriate CIDR advisors after the last resident advisor left in 1995, and it is made up of a small Malian staff of four people. The *Service Commun* is entirely funded through billing the *caisses villageoises* for its services. It receives 15 percent of the profits of each *caisse villageoise* to finance its operations. This fee is charged only when the CVECA earns positive profits. This fee structure creates compatible incentives for both the *caisse* and the *Service Commun* to work towards enhancing the profitability and sustainability of the organization.

B. Policies

The policies adopted by the *caisses villageoises* have promoted the sustainability of these village organizations without jeopardizing the depth of their outreach. This is not surprising. These policies have reflected the value that the villagers place on the permanency of their financial institution. These policies have thus reflected the opportunity cost of funds in this setting and have responded to the genuine demands of the villagers for specific financial services. These policies are described next.

1. Deposit services

The *caisses villageoises* have adopted the *savings-first* approach recommended by the CIDR. They receive no endowment of loanable funds to start their lending operations. During the first year of operation, they have to exclusively rely on deposits for their loan-granting activities.

Table 2. Operational Characteristics of the *Caisses Villageoises* in Mali, 1993-1996.

	1993	1994	1995	1996
Membership size	12,515	15,330	18,819	21,495
Members from other villages (%)	19.0	25.0	28.0	34.0
Membership annual growth (%)	--	22.5	22.8	14.2
Total deposits ^a	78,291,723	122,331,995	186,463,158	243,798,733
Deposit growth in real terms (%)	--	56.3	52.4	30.7
Average term deposit size	22,100	38,055	49,648	62,500
Number of individual depositors	1,752	2,453	2,823	2,794
Total loan amount granted ^a	128,198,529	179,961,637	284,889,474	459,374,138
Loan disbursements growth in real terms (%)	--	40.4	58.3	61.2
BNDA funds ^a	23,064,076	47,934,783	75,026,316	162,561,576
Average amount granted per borrower	14,600	21,613	33,567	49,405
Number of loans granted	8,354	9,767	11,288	13,213
Number of borrowers	5,506	6,438	7,334	8,383

Source: Unpublished records of the CIDR project in Mali. The figures were not verified by the researchers. A few inconsistencies among the data could not be removed.

Note: a: Amounts in CFAF at constant 1990 prices.

Moreover, there are no forced savings at the *caisses villageoises* and loans are not linked to deposits. The average deposit balance was CFAF 62,500 (US\$ 125) in 1996, and deposit growth was 31 percent in real terms in the same year (Table 2). Although the average size of a deposit is higher than average loan size, the small size of these transactions reflects the poverty of the clientele. A low-cost technology to handle these small transactions is required for sustainability of the organization.

The *caisses villageoises* offer several deposit products such as:

- (a) demand deposit accounts, which earn no interest, and
- (b) term deposit accounts (3-12 months), which pay 18-30 percent annual interest rates.

Term deposit accounts are by far the preferred savings instrument. They attract more than two-thirds of the total volume of deposits collected (Ouattara *et al.*, 1997). This is probably due in

part to the fact that most economic activities as well as consumption patterns are *seasonal* in the Dogon region. Most clients of the *caisses villageoises* are farmers engaged in agricultural production with highly seasonal income flows. Earnings occur several months after planting. In this environment, term deposits offer a rewarding alternative means of storing purchasing power for future use. As in most poor communities, the management of liquid reserves is a major household activity.

2. Loan services

There is no targeting by loan use or by gender at the *caisses villageoises*. Loans are granted to both men and women who are creditworthy, and no conditions are levied on the use of the funds. Loans are granted only to individuals, and they always require collateral, though non-traditional forms of collateral are used, such as animals, tools and farm implements, as well as jewelry from women.

In general, close to 40 percent of the members receive loans in a given year and have a loan outstanding at any given time. In 1996, the *caisses villageoises* granted loans to 8,383 members, for an average of CFAF 49,405 (US\$ 99) per borrower. In real terms, the rate of growth of the loans disbursed was 61 percent from 1995 to 1996 (Table 2). This rapid growth of the loan portfolio was not discouraged by the high interest rates charged, thus reflecting a strong demand for credit at the village level.

Annual interest rates on loans range from 36 to 60 percent, depending on the *caisse*. These comparatively high rates are chosen by the villagers based mainly on the informal interest rates with which they are familiar. These rates allow the *caisse villageoise* to maintain a sufficient margin (at least 20 percentage points) between the deposit and the lending rates. Interest rates at informal village groups averaged 110 percent per annum (Ouattara *et al.*, 1997).

The average term to maturity of a loan is six months. In 1995, the majority of loans (78 percent) were used in trading activities, 16 percent were used for agriculture and livestock rearing, 3 percent for social purposes, 2 percent for artisanal work, and 1 percent for seasonal migration. Agricultural loans were generally for longer terms and were issued at lower interest rates than loans to traders.

3. Contract terms and conditions

The *caisses villageoises* pay interest rates on deposits that are positive in real terms.¹⁴ Attractive remuneration of deposits creates a pool of net depositors, essential for true financial intermediation and for sufficient monitoring of management. In fact, the *caisses villageoises* were able to attract large depositors, with CFAF 137,678 (US\$ 275) as the average of these larger size deposits. These deposits came mostly from informal village groups and from big traders.

¹⁴ The *caisses villageoises* operate in a low inflation environment. Between 1990 and 1996, the average inflation rate in Mali was 5.8 percent per year.

A member is not required to make a deposit in order to receive a loan. The *caisses villageoises* attract deposits by offering attractive interest rates and ensuring the quality of service (*i.e.*, safe and confidential accounts). The policy at the *caisses villageoises* is to match the term structures of assets and of liabilities at the organization's level by trying to collect longer-term deposits (3 to 12 months) and disbursing shorter-term loans (1 to 9 months). This policy lowers the costs of liquidity management.

Interest rates vary depending on the intermediation and operating costs at the particular CVECA and on the costs of borrowing from external sources. All *caisses villageoises* keep a gross intermediation margin of at least 20 percentage points, thereby charging interest rates on loans of 36 to 60 percent per year. This margin, relatively wide compared to those of commercial banks, allows the *caisses villageoises* to cover their costs, including the payment of external auditing services, and still be profitable. Profitability is necessary to keep the right structure of incentives when there is village-wide governance.

Loans are primarily funded from member deposits and, more recently, from external borrowing from the Agricultural Development Bank of Mali (BNDA). These organizations had to turn to outside funding to address increases in loan demand compared to deposit growth. Loan disbursements increased 61 percent from 1995 to 1996, while deposits grew 31 percent over the same period, suggesting excess demand for credit at the village level (Table 2).

Despite the increased reliance on BNDA funds, whose importance grew from 18 percent to 35 percent of the loan portfolio, the *caisses villageoises* still rely heavily on deposits as the main source of funds for their loans. Given the rules for access to BNDA funds, these proportions should not change further. This matters, given the importance of depositors in balancing interests within the organization and preventing borrower domination. With the availability of funds from the BNDA, the *caisses villageoises* have also engaged in better term transformation, by granting relatively longer loans of six months or more, which are not possible otherwise, given the term structure of deposits.

C. Outreach

1. Breadth of outreach

By December 31, 1996, there were 21,950 members in 52 CVECAs in the Dogon region of Mali. This represents an average membership of 422 people per local organization. The *caisses villageoises* can reach as high as 95 percent of the adult population of a village. The reasons for this outstanding local outreach include the community-oriented focus of the CVECAs, which allows all villagers to participate in the organization and in its governance. Management committee members are continuously working on bringing in more members to the organization. The resulting diffused governance structure may conspire in the future, however, against their growth.

Another reason for the outstanding outreach is the focus of the CVECAs on savings services, which meet a widespread demand for financial services and which make the villagers feel that the *caisse villageoise* belongs to them. The incorporation of diligent depositors is an indicator of a

valuable dimension of outreach and a more robust source of institutional strength than village-wide participation in the organization.

Table 3. Financial Indicators and Operational Efficiency at the *Caisses Villageoises* in Mali, 1995-96.

	1995	1996
Financial expenses (CFAF)	29,981,265	51,095,800
Operating expenses (CFAF) ^a	5,234,010	5,680,310
Total expenses (CFAF)	35,215,275	56,776,110
Total income (CFAF) ^b	60,199,275	103,706,485
Net earnings (CFAF) ^c	24,984,000	46,930,375
Average total assets (CFAF) ^d	286,491,700	518,433,890
Average total equity (CFAF) ^d	34,188,705	58,397,920
Average total liabilities (CFAF) ^a	252,302,995	460,035,970
Average outstanding portfolio (CFAF) ^d	294,999,000	320,251,065
Operating expenses/Outstanding portfolio (%)	1.8	1.8
Operational self-sufficiency ^e (%)	170.9	182.7
Gross financial margin ^f (%)	10.5	10.1
Net operating margin ^g (%)	8.7	9.1

Source: *Caisses Villageoises* and *Service Commun* records.

Notes: *a*: Operating expenses are equal to personnel expenses and administrative expenses, including depreciation of fixed assets. They do not include financial costs and loan loss provisions.

b: Income from interest and loan fees.

c: Total income minus total expenses.

d: Averages of beginning-of-year and end-of-year balances outstanding, to compensate for the rapid growth of the amounts outstanding. Income earned (a flow) must be compared to the *average* stock.

e: Operational self-sufficiency = Financial income / Financial costs + Operating costs + Loan loss provision.

f: Gross financial margin = (Financial income - Financial costs) / Average total assets.

g: Net operating margin = Gross financial margin - Operating costs / Average total assets.

2. Depth of outreach

The *caisses villageoises* are located in one of the poorest regions of Mali. Thus, their services and especially their loans are meant for poor people in remote rural areas. Despite the absence of gender targeting, female membership at the *caisses villageoises* ranges from 20 to 50 percent, depending on the village. The average loan size of US\$ 99 is small, representing 40 percent of the country's per capita GNP. The *caisses* are able, therefore, to attain their goal of reaching poor people in Mali. The relative wealth of their members is further explored in Ouattara *et al.* (1997).

D. Sustainability

Sustainability of a microfinance organization matters (Gonzalez-Vega, 1998c). One condition for sustainability is financial self-sufficiency. The CVECAs have shown a high degree of self-sufficiency.

1. Self-sufficiency

The most basic indicator of operational efficiency examines the organization's operating expenses as a percentage of its average loan portfolio.¹⁵ This proportion reveals how much it costs the organization to lend one CFAF. High ratios may suggest administrative inefficiency, a small loan portfolio or a combination of both. The *caisses villageoises* show low ratios, with operating costs as low as 1.8 percent of the loan portfolio in 1995 and 1996 (Table 3). Operational expenses at the *caisses villageoises* are, thus, very low. This is a sign of an efficient operation and it reflects the adaptation of the organization to village conditions. Profits are generated, in turn, to cover profit-sharing arrangements with the management committee and to pay for the assistance from the *Service Commun*.

Operational self-sufficiency indicators at the *caisses villageoises* also show that these organizations more than adequately cover their operational costs with their overall revenues. The proportion was above 100 percent in 1995 and 1996. In 1996, for every CFAF 1 of operating expenses, the *caisses villageoises* generated CFAF 1.8 in income.

The performance and sustainability of a microfinance organization depends on its *financial self-sufficiency*, i.e., on its ability to generate sufficient income to cover not only its operating but also its financial expenses. In 1995 and 1996, the net operating margin of the *caisses villageoises* was positive and it reached 9.1 percent in 1996 (Table 3). A positive net operating margin indicates that the *caisses villageoises* were covering all costs with income derived from their loan operations. They were financially self-sufficient. This margin was not influenced by the presence of donor funds, because the *caisses villageoises* did not receive any grants of funds for their on-lending operations. They were, therefore, mostly independent from subsidies.

¹⁵ Given limited resources, a full financial evaluation of the system was not undertaken. These self-reported figures are presented here for illustrative purposes (orders of magnitude) only.

2. Repayment performance

Repayment performance at the *caisses villageoises* had so far been outstanding. Repayment had been maintained at a high 97 percent of amounts due over the years. These high repayment rates may reflect the creation of a *permanent* relationship of the clients with the organization, in an environment where there are not many other options to gain access to financial services. Lack of alternatives creates incentives to protect this relationship. The villagers believe that the *caisses villageoises* belong to them and make every effort to protect their integrity as a valuable village institution.

The *caisses villageoises* have also adopted a path to sustainability through the creation of *associations* supported by a *Service Commun*, which took over the support function of the implementing agency (CIDR). These associations play an important screening and monitoring role in the process of obtaining access to commercial sources of funding for the individual *caisses*.

Threats to organizational viability may come, however, from increasing dependence on these outside funds. Fortunately, the *caisses villageoises* have been able to restrict outside funding from the BNDA to less than 50 percent of their loan portfolio. Hence, reliance on deposits remains important for the *caisses*.

Nevertheless, a local savings threshold may be reached quickly in village economies facing binding *wealth constraints*, and management needs to come up with ingenious ways of generating more deposits. This requires convincing villagers, who still keep most of their savings in physical form, especially livestock, to deposit more savings with the *caisses*. For this, they need to persuade villagers of the safety and liquidity of the deposits.

E. Ownership and Governance

1. Ownership

As with other member-owned organizations, the *caisses villageoises* are characterized by the fact that there are a lot of diffused owners rather than a major owner with a vested equity capital or strong stake. Moreover, voting powers do not depend on the equity at risk. This rule destroys incentives for the right degree of internal control. Moreover, the crucial element in ownership is the ultimate power to dispose of residual claims. In the case of the *caisses villageoises*, the village is an undefined owner and the rules for allocating residual claims make the village at large the ultimate final beneficiary of the performance of the organization.

While participatory institutions tend to have deep roots, the dual role of owner and client may pose potential conflicts of interest that could threaten the sustainability of the organization. Such conflicts have not yet emerged at the *caisses villageoises*, in part because the ownership of the organization extends to the entire village (members and non-members) and village social structures are still strong. Decision-makers are all the villagers. This feature diminishes the power of members who may want to obtain private benefits at the expense of other members. The village has a vested interest in protecting the organization due to the absence of other financial alternatives. Thus, the

villagers provide effective monitoring of the *caisses villageoises*, which has prevented opportunistic behavior and ensured good repayment. The fact that these villages in the Pays Dogon region in Mali are relative small (400 to 500 adult populations) clearly facilitates effective governance.

In case any of the *caisses villageoises* were to go bankrupt, the assets would belong to the village. The villagers would decide on the reallocation of those assets. The alternatives include a community development project or a transfer of the assets to another village organization. If the *caisse* owes the BNDA any funds, it would have to repay this debt before any reallocation of the remaining assets within the village takes place.

2. Governance

The *caisses villageoises* system has a fairly flat and simple organizational and governance structure. All villagers elect a management committee to run the organization. The management committee is made up of men and women who are natural leaders. Its members are elected by the entire village for three years, with the appointment being renewable just once, for a maximum term of six years. This rule attempts to avoid any abuse and opportunistic behavior. The committee is responsible for making loan decisions. Its members receive a remuneration at the end of the year from the profits generated through the interest earnings on loan activity. This *incentive compatible* arrangement ensures that management evaluates loans carefully.

This use of performance-based incentives for management makes more sense when it is coupled with management's discretionary powers over important decisions such as screening loan applicants, deciding whether to grant the loan and for what amount, and pursuing contract enforcement. Proper incentives given to management through profit sharing are a key ingredient of the good performance of the *caisses villageoises* as well as in removing incentives for shirking and collusion.

Internal rules and regulations are reviewed yearly in a general assembly of all villagers, members and non-members. At that time, all decisions with respect to the future of the *caisse* are made, including changes in the level and term structure of interest rates as well as membership fees.

Based on the assumption that effective governance is critical for organizational performance and sustainability, it is critical to examine the extent to which authority and responsibility have been decentralized. This is accomplished next.

3. Decentralization

At the first-tier, the *caisses villageoises* are highly decentralized, independently run by managers chosen among the villagers. Governance involves the entire village during annual meetings. The villagers make all decisions on pricing deposit and loan products, profit allocation, and the election of new committee members. This approach leads to a high degree of local accountability for governance of the *caisse* and for sound lending decisions, as long as village structures are effective.

Loan decisions at the *caisses villageoises* are as decentralized as possible for reasons of efficiency. These decisions are entirely left to the loan committee in each village. Strong local involvement in selecting borrowers and in handling repayment is essential for sound credit operations, given the challenges of evaluating creditworthiness. Outsiders would have to incur high costs to overcome the inevitable information barriers.

At the second-tier level, client participation remains strong. Independent local *caisses villageoises* elect representatives to the associations. The *associations* are responsible for reviewing loan applications for outside funding for the member *caisses*. The danger of insider behavior is constrained by strict eligibility criteria for loans.

Thus, two critical elements in effective governance exist at the *caisses villageoises*. First, authority and responsibility have been decentralized from the beginning. Second, compatible incentives make management decisions contribute to the sustainability of the organization by making sustainability valuable to the decision-makers.

F. Challenges

Several elements behind the success of the *caisses villageoises* also represent the biggest challenges for the sustainability of these organizations in the future. These circumstances include:

1. Cost-effective savings-deposit mobilization

There is a limit to the amount of savings the *caisses villageoises* can mobilize within their relatively small villages, and this threshold may be quickly reached in poorer environments. Longer-term and larger volumes of savings are almost impossible to collect in this environment but are nevertheless needed to meet the demand for longer-term and larger loans. As discussed below, the *caisses villageoises* have to turn to outside funds to meet such demands and, at this point, outside funds represent 30 percent of the loan portfolio of the system.

Additional deposits may be increasingly costly to mobilize. This may be the case as the organization tries to mobilize deposits from members living in other villages. If the cost-effective frontier of going to other villages to bring in new members and depositors outweighs the benefits, it might be preferable for the *caisses villageoises* to stay within the boundaries of their own village and to devise other ways of increasing local deposits.

Convincing villagers to deposit more with the *caisse villageoise* requires that members perceive benefits from doing so. One such benefit is the positive real interest rate paid on deposits. Another incentive is the opportunity for safe-keeping of funds based on the perception that the *caisse villageoise* is a secure place, as signaled by the physical appearance of the office. In general, these offices are built to last, using durable materials such as bricks and tin roofs. Continuous improvements are being made, such as adding reinforced doors, to make them as theft proof as possible.

2. Sustained loan recovery and low costs

Village monitoring and trust protect small one-village organizations and allow them to maintain repayment rates of 97 percent of amounts due. This repayment performance is nearly impossible to achieve when the local organization expands to other villages or operates in a larger urban environment. Thus, the added screening and monitoring costs in lending to outside borrowers may outweigh the benefits of bringing such members into the organization. So far, the *caisses villageoises* have tried to reduce the risk of default from outside members by imposing more restrictions on them. Thus, an outside borrower needs a guarantor who is a resident of the village and a member of the local *caisse*, in addition to the usual physical collateral. In effect, management is keeping its monitoring role within the village boundaries by transferring this function to someone from the village.

Given the use of village mechanisms for borrower monitoring and contract enforcement, operating costs have been low, as shown in Table 4. These costs have not increased with the outstanding portfolio and are quite low compared to those incurred by other microfinance organizations.

Table 4. Consolidated Income Statement for the *Caisses Villageoises* in Mali, 1995-96.

	12-31-95	12-31-96
INCOME		
Loan Interest income	39,540,750	60,699,005
Interest receivable	20,658,525	43,007,480
TOTAL INCOME	<u>60,199,275</u>	<u>103,706,485</u>
EXPENSES		
Interest paid on deposit accounts	17,120,315	26,535,530
Interest payable	12,860,950	24,560,270
Administrative expenses	4,143,000	5,336,610
Depreciation expenses	1,091,010	343,700
TOTAL EXPENSES	<u>35,215,275</u>	<u>56,776,110</u>
NET INCOME	<u>24,984,000</u>	<u>46,930,375</u>

Source: *Caisses villageoises* and *Service Commun* reports.

Note: Amounts in CFAF.

3. Effective management of outside funds

The injection of outside funds has not yet turned out to be the threat that might have been anticipated. Access to a moderate amount of external funds has, instead, allowed the *caisses villageoises* to grant larger and longer-term loans to their members, which would have been beyond the capacity of the funding base of local deposits. To achieve this performance, the *caisses villageoises* have had to consider and answer several questions such as:

(a) When is outside money just too much?

Ideally, outside money should be kept at a level such that it does not discourage deposit mobilization. The *caisses villageoises* have put a system of requirements in place to prevent this from happening. The main constraint is tying the availability of BNDA funds to 150 percent of deposits by the *caisse villageoise* during the first two years and to 200 percent thereafter. Moreover, to be eligible for a loan, an individual *caisse villageoise* must meet the following criteria:

- (i) it has been in operation for at least a year,
- (ii) it has high quality management, and
- (iii) it has a loan default rate of less than 15 percent.

Two elements of these criteria deserve comment. First, the linkage of outside funds to the level of local deposits is an important and positive feature that protects the incentives for local deposit mobilization. The criteria of allowing access to outside money to reach 1.5 to 2 times the local deposit base does seem high, however. While this is a ceiling, and not all *caisses villageoises* reach this level, there has been a recent tendency for a rapid growth in this outside money. The evidence in Table 5 underscores the growth of BNDA debt in the total liabilities of the *caisses villageoises*, registering a greater share of total liabilities than locally mobilized deposits for 1996.

The second element is the relaxed criterion for arrears (*i.e.*, 15 percent) for qualification to access outside money through the associations. Again, this is a floor, to guarantee at least 85 percent loan recovery. In actual fact, very few *caisses villageoises* register loan recovery rates below 95 percent, and most are above 97 percent, except for some recently established *caisses* just learning to operate for the first time. Thus, the 15 percent criterion is largely unimportant and non-operative. Still, it would be more sound to establish a more rigorous eligibility criterion, more in line with the actual performance of the *caisses* themselves. This is particularly important when a rapidly growing portfolio masks the relative importance of arrears.

Table 5. Consolidated Balance Sheet Data for the *Caisses Villageoises* in Mali, 1995-96.

	12-31-95	12-31-96
ASSETS		
Cash	33,441,335	35,585,220
Interest receivable	20,658,525	43,007,480
Loan portfolio	222,118,840	418,383,290
Due from banks (deposits)	10,273,000	21,457,900
TOTAL ASSETS	<u>286,491,700</u>	<u>518,433,890</u>
LIABILITIES AND EQUITY		
BNDA debt	99,785,000	232,108,000
Guarantee fund	3,013,415	4,883,295
Credit fund	13,362,100	24,972,545
Term deposit accounts	113,283,885	158,512,180
Passbook accounts	9,997,645	14,999,680
Interest payable	12,860,950	24,560,270
Total Liabilities	<u>252,302,995</u>	<u>460,035,970</u>
Equity	9,795,235	12,483,960
Previous year income (loss)	-590,530	-1,016,415
Year-end Net Income	24,984,000	46,930,375
Total Equity	<u>34,188,705</u>	<u>58,397,920</u>
TOTAL LIABILITIES AND EQUITY	<u>286,491,700</u>	<u>518,433,890</u>

Source: *Caisses villageoises* and *Service Commun* reports. Self-reported, unverified figures.

Note: Amounts in CFAF.

(b) What incentives will the *caisses villageoises* have to mobilize deposits aggressively?

As pointed out above, the outside loan criteria generally encourage each *caisse villageoise* to pursue an aggressive deposit mobilization policy and to keep a good flow of deposits at the local level. These criteria also ensure repayment to the outside creditor as only creditworthy, good performing *caisses villageoises* are eligible for outside funding. Meeting the revealed preference of members (transforming latent into effective demand) with new products such as bigger and longer-term loans and repeat loans, as made possible by the outside funds, induces voluntary contract compliance, which translates into high loan repayment rates of 97 percent of the amounts due.

There has been no negative growth in the amount of deposits mobilized. In fact, deposits have grown faster than the membership. Thus, while the membership grew 22 percent in 1994 and 1995 and 14 percent in 1996, in real terms deposits grew 56 percent in 1994, 52 percent in 1995, and

31 percent in 1996 (Table 3). Deposits have been increasing at a decreasing rate, however, probably because some village threshold may have been reached. Growth remains brisk, nevertheless, which is encouraging for the future of these organizations.

4. The PARMEC law challenge

The PARMEC law is one of the biggest challenges the *caisses villageoises* have to face. The worst threat comes from the interest rate cap on loans. Other requirements under the law, such as reporting, data collection, and reserve requirements are already being followed by the *caisses* with the help of the *Service Commun* and will not be a hindrance on the performance of these organizations. Although Mali approved the PARMEC law in August 1994, the law has not been vigorously enforced. The hope is that intense domestic and international debate on its likely negative consequences may trigger welcome changes in the near future.

THE NIGER CREDIT UNION MOVEMENT

A. Introduction

Credit unions (CUs) are thought to have originated in Germany, with the advent of the Raiffeissen societies in the Nineteenth Century. Friedrich W. Raiffeissen created the cooperative credit institutions to help the poor and the needy and as charitable organizations. As they became more self-help oriented, the credit societies grew rapidly throughout Europe, to give rise to the credit union movement as it is known today throughout the world.

The World Council of Credit Unions (WOCCU) is the worldwide organization of CUs and similar cooperative financial institutions. Members of WOCCU include seven regional and national credit union confederations serving Africa, Asia, Australia, Canada, the Caribbean, Latin America, and the United States. There are four free-standing leagues representing Fiji, Great Britain, Ireland, and New Zealand.

By December 1996, there were 36,244 CUs in the world, with a membership of more than 89 million people, and a penetration rate of 6.65 percent of the population (WOCCU statistical report).¹⁶ Deposits were estimated at US\$ 331 billion, loans at US\$ 253.6 billion, reserves at US\$ 36.1 billion, and assets at US\$ 379.3 billion.

The African Confederation of Cooperative Savings and Credit Associations (ACCOSCA) is a WOCCU member. It gathers CUs from 28 countries. Its headquarters are in Nairobi, Kenya. ACCOSCA is comprised of 4,478 organizations, with 2.5 million members, US\$ 481.9 million in deposits, US\$ 396.1 million in loans, US\$ 18.8 million in reserves, and US\$ 523.1 million in assets. The penetration rate was 1.75 percent for African CUs, considerably lower than in other parts of the world.

In Africa, CUs have been primarily sponsored by organizations such as WOCCU, Développement International des Jardins (DID) from Canada, and Crédit Mutuel of France. The sections below review the Niger credit union movement as an example of how WOCCU has applied its latest technology and innovations in an African environment.

B. General Background

The credit union movement in Niger was started by WOCCU as a pilot project in 1990 in response to recommendations by a research team from The Ohio State University (Graham and Cuevas, 1990). The study by the OSU team in 1986-87 had found that there were no formal financial

¹⁶ The *population penetration rate* is measured with respect to the working-age population of WOCCU member countries.

institutions outside of the main urban areas of Niger (Graham *et al.*, 1987). Instead, rural households had to rely almost exclusively on sources to satisfy their demand for financial services.

The project for the development of CUs or *caisses populaires d'épargne et de crédit* (CPECs), as they are called in Niger, started in the department of Zinder in 1990. The first three-and-a-half years of the pilot phase were devoted to developing and promoting CUs in Zinder, where 11 CPECs were created during that period. During the second and last phase (1992-1997), the objective of the project funded by the United States Agency for International Development (USAID) was to promote and extend CPEC development in other departments.

As of April 30, 1997 there were 65 CPECs in six out of eight departments in Niger (Zinder, Maradi, Niamey, Kollo, Tillabery, and Dosso). These CPECs had 12,700 members, of whom 35 percent were women. The movement had accumulated CFAF 450 million (US\$ 900,000) in assets, CFAF 400 million (US\$ 800,000) in deposits, and CFAF 190 million (US\$ 380,000) in loans outstanding.¹⁷

At the end of the project in June 1997, WOCCU handed over the CPECs to the national association, *Mouvement des Caisses Populaires d'Épargne et de Crédit* (MCPEC), whose primary mission is to create a fully functional central financing facility that would intermediate funds between the deficit and surplus units of the movement.

C. Institutional Design

Credit unions are organized under rules and regulations that are fairly uniform wherever they exist, and the Niger CPECs are no exception. The CPECs are member-owned, member-operated, non-profit organizations that operate as cooperative financial institutions.

Credit unions have a common bond that links their members. In open-bond or community-based CUs, members are from the same community, village, or area of residence. In occupational or closed-bond CUs, members belong to the same profession, are engaged in the same occupation, or work in the same company. Thus, occupational CUs have a more homogeneous membership than community-based credit unions. Most credit unions in developed countries are closed-bond organizations, while most credit unions in developing countries are open-bond organizations. In Niger, most CUs are open-bond entities, *i.e.*, community-based organizations.

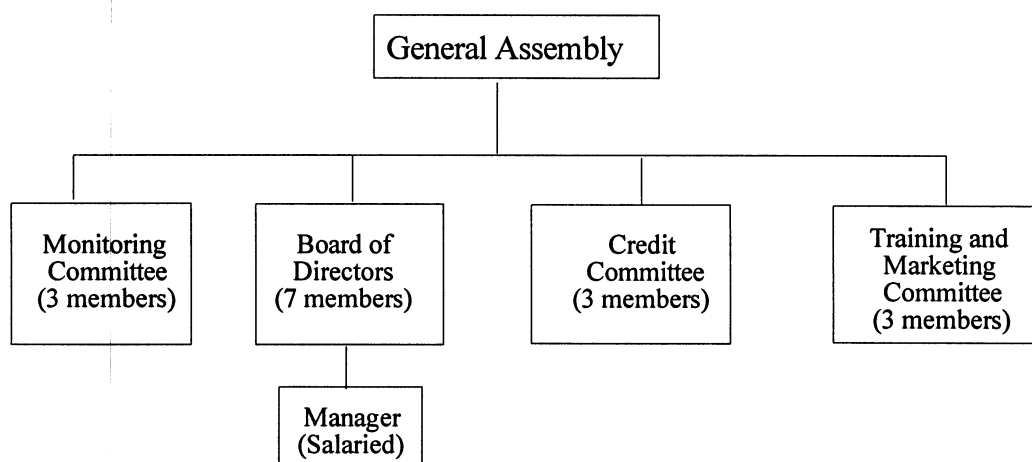
Each CPEC is run by a management committee of 16 members, on average, and one salaried manager (see Figure 2). The committee comprises a board of directors (seven members), a credit committee (three members), a loan monitoring committee (three members), and a training and marketing committee (three members). The cashier or general manager is the only paid employee.

The credit committee analyzes all loan requests and makes the final decision on granting loans. Large size loan requests (greater or equal to CFAF 200,000 or US\$ 400) are submitted to the board of

¹⁷ US\$ 1 = CFAF 500

directors for final approval. On average, one-third of management committee members are women in CPECs with mixed (male and female) membership. One-third of all CPECs have an all female membership base for religious reasons that would not allow men and women to belong to the same organizations (orthodox muslims). The manager of a CPEC is responsible for the day-to-day decisions, while the ultimate control of the organization belongs to the general assembly of member-owners.

Figure 2. Generic Organizational Outline of Credit Unions (CEPCs) in Niger 1996.



D. Policies

1. Membership policy

Membership in the Niger CPECs is open to all community-based members. Most CPECs in Niger are community-based with a few in urban areas that are occupation-based (closed-bond) CPECs. Minimum membership fee requirements are CFAF 2,500 (US\$ 5) in rural areas and CFAF 3,500 (US\$ 7) or higher in urban areas. The highest membership fee was CFAF 9,500 (US \$19) at an urban CPEC. Some rural CPECs allow the membership fee to be paid in small increments. Membership fees include a minimum deposit of CFAF 500 (US\$ 1) which buys the member a share. This allows even the poorest to become members.

2. Share capital

Individual share capital in Niger CPECs cannot be traded or sold to others outside of the organization. Members get restitution of their shares upon resignation from the credit union. The return on share capital is quite low in the Niger CPECs, although most organizations do pay dividends by distributing profits to members. Interest rebates on loans are not an option to reward members at the Niger CPECs. This policy prevents these organizations from turning into borrower-

dominated credit unions, with net borrowers trying to obtain private benefits from other members by lowering interest rates on loans below a sustainable level.

3. Lending policies

Niger CPECs mobilize deposits from their members and provide loans to their members only. The member's share ownership is crucial in determining eligibility for credit and the size of loan. In general, credit union members have a right to borrow a multiple of their share, frequently two to one (2:1). In Niger, deposit accounts are used, in addition to shares, as the basis to establish the loan multiple of 2 to 1, for at least the first year of operation. There is also a formal limit on the size of a single loan.

Credit policies are similar in all CPECs and are generally more stringent during the first year in which the organization engages in credit activities. These initial requirements include:

- (a) a minimum deposit of CFAF 5,000 is required to apply for a loan;
- (b) at least three months membership is required;
- (c) a member has rights to a loan equivalent to a multiple of his/her deposit (frequently 2:1); and
- (d) a co-signor who is also a member is required for any loan and must have sufficient funds in his/her savings account to cover the entire amount of the loan.

After one year of activity, the CPECs can revise their loan policies. Thus, loan multiples can change from 2:1 to 3:1. This reduces the effective interest rate implicitly charged on the net proceeds of the loan. The effective rate is twice the contractual rate when the multiple is only 2:1 and one-and-a-half times the contractual rate when the multiple is 3:1.

Most CPECs also find the co-signor requirement to be too restrictive and have already revised their loan policies to include acceptable tangible collateral. At this point, different CPECs accept land and other physical assets as collateral. In women-only CPECs, gold jewelry and woven clothing materials are also accepted as collateral. In the second year of loan activity, the value of the collateral should cover 75 percent of the loan amount, while 50 percent should be covered in the third year and beyond. The collateral required needs to be a credible threat for contract enforcement. In this environment, with limited opportunities for formal contract enforcement, tangible collateral is inferior to a member's cosigning. Thus, the CPECs are taking more risks and would need to monitor their borrowers more closely to avoid any rise in default.

E. Lending Technologies

Loans from the CPECs are granted to individuals only. There are no group loans. Loan characteristics are fairly similar across CPECs. The maximum amount that can be granted to a single member depends on the CPEC, and it varies from CFAF 100,000 (US\$ 200) to CFAF 1 million (US\$ 2,000). In some CPECs, not more than 10 percent of the loan portfolio can be given as a loan to a single individual.

In general, 70 percent of member deposits constitute the CPEC loanable fund base. The rest is kept as reserves. In case of a liquidity shortage, all loan activity is terminated until additional loans outstanding are repaid. There have been instances of credit rationing due to a lack of funds in some CPECs. In some cases, not all members manage to get loans. In other cases, loan amounts disbursed are below the amounts authorized. Sometimes, after a liquidity shortage, priority is given to smaller loan applicants, as is often the case. This encourages members to demand smaller loan amounts in order not to be excluded. More vigorous deposit mobilization from net savers would reduce the incidence of these shortages.

While some CPECs are short on liquidity, others, especially women-only CPECs, are frequently surplus units. It was expected that these CPECs would benefit from the intermediation role of the central finance facility. Women are known to be net savers in Africa and to value deposit services more than loans. The Niger CPECs place their excess liquidity with other financial institutions, *e.g.*, commercial banks. It was believed that a central finance facility that intermediated funds between deficit and surplus units would offer the CPECs another alternative and likely better returns on their investments (in the mid 1990s, commercial banks in Niger were paying no interest on deposits). The central finance facility would lend directly to credit unions for a fee and would find the best investment alternatives for the liquidity it manages. This expectation assumes an independent central finance facility with superior financial management expertise.

All loans carry a 2 percent per month interest charge on the balance outstanding. Most loans usually require monthly installment payments of principal plus interest. Penalties (2 percent of principal due) are applicable in case of late payments. In special cases (loans for cattle rearing, for example) repayment of principal is due only at the end of the loan term (5-7 months), with interest payments still due every month. An application fee is also required with a loan application. The fee varies from 1 to 3 percent of the loan amount depending on the CPEC. When all interest costs and fees are taken into account, the effective interest rate in the CPECs varies from 48 to 54 percent per annum. These rates are not very different from those charged by the *caisses villageoises* in Mali, where no savings requirements exist and which grant smaller loans.

Given a nominal annual interest rate in all CPECs of 24 percent, a 2:1 loan multiple, and a loan application fee of 1-3 percent of the loan, the effective rate of interest can be estimated using the formula developed by Poyo (1989) for the Dominican Republic CU movement. The formula is:

$$R_E = \frac{(R_N + T_C - I_S \phi)}{(1 - \phi)}$$

where:

- R_E = effective interest rate charged on loans,
- R_N = stated nominal rate of interest on loans,
- T_C = explicit transactions costs as a percentage of the loan amount,
- I_S = expected interest rate on savings paid by the credit union, and
- ϕ = one over the loan multiple.

There are no targeted loans in the Niger CPECs. Management is fully aware that money is fungible. Thus, loans in the CPECs are granted for a variety of purposes such as naming ceremonies,

weddings, health care, funerals, and school fees as well as for production purposes such as buying seed and inputs, or cattle rearing. The majority of loans are granted for a year or less, and the average term to maturity of a loan in all CPECs is five months.

All CPECs offer deposit services to their members. Individual members as well as groups can open a savings account at a CPEC. In addition to passbook current accounts, CPECs also have offered their members interest-bearing deposit accounts since 1996. Guarantee funds offered as additional collateral also earn interest at the CPECs. Members are rewarded at the end of the year when profits are redistributed and members receive a dividend proportional to their savings. Interest-bearing deposit accounts, introduced in 1996, were an effort by management to encourage savings, especially from women, known to be potential net savers. When an organization relies heavily on deposits for its lending activity, it is essential to find ways to generate a continuous and increasing flow of deposits to meet loan demand.

F. Outreach and Growth

1. Breadth of outreach

The Niger CPECs had achieved substantial growth and excellent results, exceeding all expectations and earlier projections (Ouattara *et al.*, 1996b). Up to 1995, membership grew at a rate of over 100 percent per year, as more than 10 CPECs were being created every year (Table 6). As of April 30, 1997, there were 65 CUs with 12,700 members, of whom 35 percent were women. A small proportion of the membership (2 percent) was made up of groups. Thus, average membership per CPEC was 195 members.

Table 6: Composition and Growth of CPEC Membership in Niger, 1990-1996

End of year	Numbers and Annual Rate of Growth (%)				Shares (%)			
	Men	Women	Groups	Total	Men	Women	Groups	Total
1990	453	57	3	513	88.3	11.1	0.2	100
	--	--	--	--				
1991	476	73	4	553	86.1	13.2	0.7	100
	(5.1)	(28.1)	(33.3)	(7.8)				
1992	691	280	8	979	70.6	28.6	0.8	100
	(45.2)	(283.6)	(100.0)	(77.0)				
1993	1,554	496	26	2,076	74.9	23.9	1.2	100
	(124.9)	(77.1)	(225.0)	(112.1)				
1994	3,293	1,486	59	4,838	68.1	30.7	1.2	100
	(111.9)	(199.6)	(126.9)	(133.0)				
1995 ^a	3,711	1,617	62	5390	68.4	30.0	1.5	100
	--	--	--	--				
1995	7,169	3,431	125	10,725	66.8	32.0	1.2	100
	(117.7)	(130.9)	(111.9)	(121.7)				
1996	8,385	3,726	229	12,340	67.9	30.2	1.9	100
	(17.0)	(8.6)	(83.2)	(15.1)				

Source: WOCCU/Niger data base.

Notes: Percentages in parentheses are annual rates of growth.

a: For March 31, 1995.

-- Not applicable.

Loans outstanding, the number of loans, and deposits all grew rapidly in real terms, at more than 100 percent per year since the inception of the program. By April 1997, a total of CFAF 400 million (US\$ 800,000) had been mobilized in deposits, and there were 1,200 loans outstanding for CFAF 190 million (US\$ 380,000). Accumulated, CFAF 650 million (US\$ 1.3 million) had been granted as loans to 7,000 members, of whom 40 percent were women, from the beginning of the program.

2. Growth in assets, member deposits, and shares

Growth in assets, deposits, and shares was impressive. In April 1997, the CPECs in Niger had accumulated CFAF 450 million in assets, surpassing the target of CFAF 128 million. In real terms, rates of growth in assets averaged over 100 percent per year from 1990 to 1996 (Table 7). Growth in savings deposits was even more dramatic, from CFAF 1 million in 1990 to CFAF 183.7 million in 1996. Despite the devaluation of the CFAF, a real deposit growth of 244.5 percent per year was recorded in 1994, when CPEC membership increased by 133 percent. Due to the CPEC policy of allowing only one share per member, shares in the CPECs have only kept up with a similar increase in membership, averaging, nevertheless, a rate of 82 percent annual growth over the years.

Table 7: Growth in Assets, Deposits, and Shares in Real Terms for Niger CPECs, 1990-1996

End of Year	Amounts ^a			Annual Rate of Growth (%)		
	Assets	Deposits	Shares	Assets	Deposits	Shares
1990	2,737,440	1,052,050	517,250	--	--	--
1991	4,467,012	2,589,501	600,678	63.2	146.1	16.1
1992	13,403,654	8,116,894	1,455,772	200.1	213.5	142.4
1993	31,942,623	20,062,669	3,029,638	138.3	147.2	108.1
1994	110,031,672	74,668,563	4,926,280	244.5	272.2	62.6
1995	213,817,500	157,923,492	9,179,053	94.3	111.5	86.3
1996	259,499,729	183,704,374	10,194,942	21.4	16.3	11.1

Source: WOCCU/Niger data base.

Notes: ^a Amounts measured in CFAF at constant 1990 prices.

-- Not applicable.

3. Growth in loans

In 1996, the Niger CPECs granted 1,935 loans for a total amount of CFAF 183.7 million of constant 1990 purchasing power. This implies an average loan size of CFAF 94,935 (US\$ 190). The loan amounts granted ranged from a minimum of CFAF 5,000 to a maximum of one million. The growth in the number and amount of loans granted was remarkable (Table 8). The loan to savings ratio went from 8.7 percent in 1992, when the organizations first started granting loans, to 48.6 percent in 1994, and to 75 percent in 1996. Average loan size increased 49 percent from 1994, when

it was CFAF 63,805 of constant 1990 purchasing power. As predicted in the OSU report, the creation of CPECs in active urban areas since then has generated demand for not only more loans but larger loans as well (Ouattara *et al.*, 1996a).

Table 8. Real Growth of the Niger CPECs Outstanding Loan Portfolio (1993-1996)

End of year	Number of loans outstanding	Outstanding balances in constant 1990 CFAF	Real rate of growth (%)
1993	68	2,264,201	--
1994	430	36,270,774	1,501.9
1995	1,185	102,993,704	184.0
1996	1,144	93,666,407	9.1

Source: WOCCU/Niger data base.

4. Depth of outreach

With an average loan size of US\$ 190 and a ratio of average loan size over GDP per capita of 73 percent, the CPEC movement in Niger is undoubtedly reaching the poor, although not the poorest of the poor. Women constituted 30 percent of the CPEC membership and received almost 40 percent of all loans granted. The average female loan size remained smaller, however, at CFAF 76,000 compared to an average loan size of CFAF 113,000 for men (Ouattara, 1996).

Female membership has remained at 30 percent since 1994. Most CPEC members are those men among the economically active poor in rural areas, where most CPECs are located. They are mostly farmers or microentrepreneurs. As of December 31, 1996 the average deposit amount in passbook accounts for all CPECs was CFAF 13,888 (US \$ 28). This is an indicator of the poverty of their members.

G. Sustainability

1. Repayment performance

The CPEC movement had a loan recovery record of 95 percent of total outstanding loans before 1996. However, 34 percent of loans outstanding were in arrears in 1996 (Table 9). As a result, management had to increase loan loss reserves 46-fold as a precautionary measure. This increase in arrears was a threatening development. Arrears constrain liquidity and make it impossible to respond to loan demand. The inability to respond to demand in turn weakens incentives to repay loans, leading to additional arrears. Demonstration effects further feed delinquency. Credit unions that do not attract net depositors are very vulnerable to these effects.

Table 9: Time Profile of Loans Granted, Repaid, and in Arrears in the Niger CPEG (1993-1996)

End of year	Number of loans outstanding	Balances outstanding (in CFAF)	Loan amount not in arrears (%)	Loan amount 0-2 months in arrears (%)	Loan amount 2-6 months in arrears (%)	Loan amount 6-12 months in arrears (%)	Loan amount more than 12 months in arrears (%)
1993	68	1,969,855	65.5	19.5	10.1	4.9	0.0
1994	430	42,944,596	72.1	22.6	5.3	0.0	0.0
1995	1,185	134,818,758	72.0	17.2	9.9	0.8	0.1
1996	1,144	129,072,309	65.7	5.3	15.3	10.1	3.6

Source: WOCCU/Niger data base.

2. Self-sufficiency: PEARLS

WOCCU created a rating system for CUs to be used as a management as well as a supervisory tool. The credit union performance rating system is now based on PEARLS (Protection, Effective financial structure, Asset quality, Rate of return and costs, Liquidity, and Signs of growth). It is similar to the CAMEL system (Capital adequacy, Asset quality, Management quality, Earnings record, and Liquidity position) used to assess the performance of banks.

The PEARLS system uses 36 financial ratios to assess the viability of the CU as a cooperative financial institution (see Annex 2 to this chapter). Operational efficiency in the PEARLS system is measured by ratios such as R_7 (Total Gross Income Margin/Total Average Assets) and R_{10} (Net Earnings/Average Total Assets). The R_7 measures the total income margin generated before subtracting overhead expenses, loan loss provisions, and other extraordinary items. In Niger, the R_7 increased from 2.0 percent in 1990 to 11.6 percent in 1994 (Shaw, 1998). In 1996, the R_7 was 14 percent, an indication of the CPEGs' increasing ability to generate sufficient income to cover operational (overhead) expenses.

The R_{10} measures the average income yield for productive assets in the balance sheet. An R_{10} of 14 percent was recorded in 1996, indicating decent net earnings by the Niger CPEGs. In addition, the return on assets (ROA) of 8.6 percent and return on equity (ROE) of 37 percent in 1996 are above industry standards of a 2 percent minimum for ROA and at least 15 percent for ROE (Table 10). Financial self-sufficiency is the ability to generate sufficient income to cover operational and financial costs of the organization. Financial self-sufficiency can be captured by the *net operating margin*. After several years of negative net operating margins, in 1996 this ratio finally reached a positive 1.7 percent in the Niger CPEGs (Table 10). A positive, although very small net operating margin reveals that the Niger CPEGs are finally covering their costs with income derived from their loan operations.

Table 10. Financial Indicators, Profitability, and Efficiency Measures for the CPFC Movement in Niger, 1993-1996.

	1993	1994	1995	1996
Financial expenses (CFAF)	850,000	5,920,000	7,739,338	249,072
Operating expenses (CFAF) ^a	1,839,233	11,562,464	26,965,213	25,980,967
Total expenses (CFAF)	2,689,233	17,482,464	34,704,551	26,230,039
Financial income ^b	621,608	6,503,035	21,240,712	31,529,593
Operating income	2,560,677	12,199,660	32,357,361	34,845,959
Total income (CFAF)	4,082,667	21,564,904	52,320,031	53,557,469
Net income (CFAF)	1,393,434	4,082,440	17,615,480	27,327,430
Financial assets	22,789,017	104,734,253	244,737,272	317,916,878
Average total assets ^c	19,840,543	79,042,121	205,047,940	318,738,867
Average total equity ^c	6,712,951	21,757,374	49,197,826	73,892,118
Total liabilities ^c	18,499,322	94,354,103	212,095,641	255,653,064
Average outstanding portfolio (CFAF)	129,437,205	22,457,226	88,881,677	131,945,534
Operating expenses/average outstanding portfolio (%)	1.4	51.5	30.3	19.7
Operational self-sufficiency ^d (%)	23.1	37.2	61.2	120.2
ROA ^e (%)	7.0	5.2	8.6	8.6
ROE ^f (%)	20.8	18.8	35.8	37.0
Gross financial margin ^g (%)	-1.2	0.7	6.6	9.8
Net operating margin ^h (%)	-10.4	-13.9	-6.6	1.7

Source: WOCCU/MCPEC report

Notes: *a*: Operating expenses are equal to personnel expenses, and administrative expenses, including depreciation of fixed assets. They do not include financial costs and loan loss provisions.

b: Financial income = income from interest and loan fees.

c: Average of first-of-year and end-of-year balances.

d: Operational self-sufficiency = Financial income / Financial + Operating Costs + Loan loss provision.

e: ROA = Net income / Average total assets.

f: ROE = Net income / Average total equity.

g: Gross Financial Margin = (Financial income - Financial costs) / Average total assets.

h: Net Operating Margin = Gross financial margin - Operating costs / Average total assets.

Another indication of the sustainability of microfinance organizations is the extent to which they rely on outside assistance for their operations. This can be measured by the Subsidy Dependence Index (SDI). The SDI measures the percentage increase in the average on-lending interest rate required to compensate an organization for the elimination of subsidies in a given year while keeping

its return on equity equal to the approximate non-concessional borrowing cost. The index assumes, for simplicity, that an increase in the on-lending interest rate is the only change made to compensate for the loss of subsidy. An SDI of zero assumes that an organization has achieved full self-sustainability. An SDI of 100 percent indicates that a doubling of the average on-lending interest rate is required if subsidies are to be eliminated (Yaron, 1994).

The SDI figures obtained using the information from published financial statements indicate that in 1996, an increase of 12.1 percent in the on-lending interest rate or a 3 percentage point increase would be required to eliminate the subsidy received by the Niger CPEC movement (see Annex 1 to this chapter). That is, the CPECs would have to increase their nominal interest rate from 24 to 27 percent to eliminate all subsidies. This is quite a modest increase from the interest rates the CPECs are currently charging on loans. The possibility of such an increase would be highly dependent, however, on the PARMEC law, which sets a cap on the interest rates microfinance organizations can charge on loans. Under the present law and a cap of 30 percent in effect in 1996, the Niger CPECs would have been able to implement the interest rate policy needed to become independent from subsidy.

H. Ownership and Governance

Niger CPECs are member-owned and member-operated organizations. While paid managers are responsible for the day to day decisions, the ultimate control of the organization belongs to the general assembly of member-owners.

In general, the owner-client structure of CUs can create conflicts among borrowers, depositors, and management. Opposition between net borrowers and net depositors for control of the organization can lead to a borrower-dominated or depositor-dominated CU. In a borrower-dominated CU, although they are usually a small segment of the membership, the net borrowers capture control of the CU, to obtain private benefits at the expense of other members, *i.e.*, net depositors. They seek private benefits by pressuring for the adoption of low interest rates, relaxed collateral requirements, and less rigorous loan recovery practices.

The Niger CPECs had so far managed to avoid this rent-seeking behavior and to stay neutral, *i.e.*, not favoring one group over the other. They had avoided borrower domination by being mandated to adopt collateral requirements and interest rate policies that do not subsidize net borrowers.

The CPEC governance is characterized by a democratic structure with a one person, one vote rule, which implies that voting powers cannot be accumulated by individuals regardless of how many shares they own. CPEC members also remain the sole residual claimants of the assets of the organization. Unfortunately, democratic control in a credit union may not result in optimum levels of monitoring and internal control (Chaves, 1994). The collective action of a majority of members can bias the allocation of credit in detriment of depositors. This threat constrains the potential growth of deposits. In an effort to compensate for these inadequate incentives, in the Niger CPECs, managers are paid employees of the organization. This has been positively correlated with

performance (Ouattara *et al.*, 1996a). Also, an increasing number of net depositors, attracted by the new savings products, will help in overcoming these governance weaknesses.

I. Issues for the Future

After seven years of activities, the Niger credit union movement finally achieved financial self-sufficiency in 1996. The movement is still dependent, however, on operational subsidies. WOCCU believes that the movement still needs three-to-five years of technical assistance and training to achieve full maturity. This situation is consistent with the experience of the *caisses villageoises*, which needed 11 years to evolve into a long-awaited status of mature organizations.

According to the results of an OSU study, several elements have positively affected the performance and sustainability of the Niger CPECs (Ouattara *et al.*, 1996b). In particular, CPEC members are comfortable with the use of market rates of interest, which are crucial in determining the long-term sustainability of the CPECs in Niger. Encouraging more deposits from members, especially women, generating larger loan portfolios, and good repayment performance will allow the CPECs to remain financially self-sufficient. Attracting more women will positively influence the organizations, as women appear to value savings even more than they value loan services.

Nevertheless, one final issue merits comments in these closing remarks. In the final year of documentation (1996), there was a notable decline in the rate of growth of loans, deposits, and share capital (Tables 7 and 8). Further evidence presented in Table 9 shows a rising rate of arrears in 1996. Moreover, a non-negligible share of these total arrears are aging, implying the threat of default. The decline in growth is not surprising for a movement entering the sixth year of activity. A rise in the aging of arrears, however, is another matter. This situation suggests that the sustainability of the movement was really not guaranteed.

Additional financial information on the Niger CUs is shown in Table 11 (consolidated balance sheet) and Table 12 (consolidated income statement). These data show that growth was brisk through 1995, followed by stagnation in 1996. Very rapid growth of the loan portfolio in 1995 was followed by some reduction, while deposits continued to grow unabated and new liabilities were issued. The arrears observed in 1996 may have thus resulted from too rapid growth. Because of these arrears, reserves for loan losses substantially increased in 1996.

Table 11. Consolidated Balance Sheet for the CPEC Movement in Niger, 1993-96 (CFAF)

	12-31-93	12-31-94	12-31-95	12-31-96
ASSETS				
Cash and cash equivalents	20,614,842	61,002,456	109,082,897	175,436,914
Accounts receivable	198,000	0	0	13,403,175
Loans	1,969,855	42,944,596	134,818,758	129,072,309
Interest receivable	5,330	787,201	835,617	0
Miscellaneous receivables	990	0	0	4,480
Financial assets	22,789,017	104,734,253	244,737,272	317,916,878
Fixed assets (building and equipment)	5,086,451	25,474,520	35,149,835	39,673,749
TOTAL ASSETS	27,875,468	130,208,773	279,887,107	357,590,627
LIABILITIES AND EQUITY				
Deposits (savings)	18,440,597	92,918,078	206,721,851	253,144,628
Interest payable	0	1,435,000	5,366,015	0
Other liabilities	58,725	1,025	7,775	2,508,436
Legal reserves	97,279	515,928	1,642,916	4,032,048
Contribution to construction	315,000	625,275	874,775	1,545,200
Credit loss reserve	38,599	123,988	1,441,003	5,768,803
Other reserve	0	0	26,600	6,613,449
Total Liabilities	18,950,200	95,619,294	216,080,935	273,612,564
Shares	2,652,285	5,831,715	12,015,380	14,048,630
Retained earnings	130,058	74,979	210,752	4,418,249
Year-end net income	1,436,024	4,082,440	17,615,480	27,327,430
Equipment subsidy	4,706,901	24,600,345	33,964,560	38,183,754
Total Equity	8,925,268	34,589,479	63,806,172	83,978,063
TOTAL LIABILITIES AND EQUITY	27,875,468	130,208,773	279,887,107	357,590,627

Source: WOCCU-Niger reports.

Table 12. Consolidated Income Statement for the CPEC Movement in Niger, 1993-96 (CFAF)

	12-31-93	12-31-94	12-31-95	12-31-96
INCOME				
Loan interest income	454,389	4,960,635	15,860,620	26,486,023
Penalty interest income	4,930	236,828	1,538,267	1,772,493
Interest from bank placements	111,719	395,657	1,193,035	330,846
Interest from central finance facility	0	0	0	3,838
Loan application fees	50,570	909,915	2,648,790	2,936,393
Entry fees	1,222,100	3,004,485	6,269,415	2,662,110
Miscellaneous income	716,969	2,692,140	4,847,234	654,256
Operational subsidies	1,521,990	9,365,244	19,962,670	18,711,510
TOTAL INCOME	4,082,667	21,564,904	52,320,031	53,557,469
EXPENSES				
Materials	623,998	2,876,171	5,171,698	625,750
Travel expenses	12,582	232,445	445,548	777,970
Training expenses	0	0	0	13,325
Meeting expenses	21,490	56,300	237,580	636,231
Promotion expenses	484,550	2,203,260	3,116,695	2,289,565
Contributions and grants	0	0	0	49,530
Maintenance expense	0	0	769,250	0
Miscellaneous losses	0	395	15,802	48,589
Salary expenses	146,000	3,371,235	9,655,400	12,923,155
Interest expenses	850,000	5,920,000	7,739,338	249,072
Depreciation expenses	0	969,250	3,229,445	0
Miscellaneous expenses	550,613	1,853,408	4,323,795	8,616,852
TOTAL EXPENSES	2,689,233	17,482,464	34,704,551	26,230,039
NET INCOME	1,393,434	4,082,440	17,615,480	27,327,430

Source: WOCCU-Niger reports.

ANNEX 1

Subsidy Dependence Index

The formula for the subsidy dependence index (SDI) is:

$$SDI = \frac{S}{LP * i}$$

where:

$$S = A(m - c) + [(E * m) - p] + K$$

and:

- S = annual subsidy received by the organization;
- A = organization concessional borrowed funds outstanding (annual average);
- m = interest rate the organization would be assumed to pay for borrowed funds if access to borrowed concessional funds were eliminated;
- c = weighted average annual concessional rate of interest actually paid by the organization on its average annual concessional borrowed funds outstanding;
- E = average annual equity;
- P = reported annual profit, before tax (adjusted, when necessary, for loan loss provisions, inflation);
- K = the sum of all other annual subsidies received by the organization (such as partial or complete coverage of operational costs);
- LP = average annual outstanding loan portfolio of the organization; and
- i = weighted average on-lending interest rate earned on the loan portfolio.

Table 13. SDI Estimates for the CPEC Movement in Niger, 1994-96

Item	1994	1995	1996
Concessional borrowing = A^a	0	0	0
Concessional rate of interest paid = c (%)	0.0	0.0	0.0
Market lending rate = m (%)	16.75	16.75	16.75
Annual average equity = E^b	21,757,374	49,197,826	73,892,118
Subsidy on equity = $(E*m)$	3,644,360	8,240,636	12,376,930
Profits = P (losses)	4,082,440	17,615,480	27,327,430
Grants and Benefits = K^c	9,365,244	19,962,670	18,711,510
Total subsidy = S	8,927,164	10,587,826	3,761,010
Revenue from lending = $LP*i^d$	6,107,378	20,047,677	31,194,909
SDI (%)	146.2	52.8	12.1

Source: CPECs financial statements

Note: *a*: No concessional borrowing took place.
b: All amounts are in CFAP.
c: Reported figures in the income statement.
d: Revenue includes loan interest income, penalty interest income, and revenues from loan application fees.

ANNEX 2

List of Performance Indicators Comprising the PEARLs Tool.

P = Protection

- P₁ Provision for Loan Losses/Delinquency >12 months
- P₂ Provision for Loan Losses / Total Delinquency

E = Effective Financial Structure

- E₁ Loans / Total Assets
- E₂ Stock and Bonds Investments / Total Assets
- E₃ Other Investments / Total Assets
- E₄ Liquid Cash Investments / Total Assets
- E₅ Deposits / Total Assets
- E₆ External Borrowing / Total Assets
- E₇ Shares / Total Assets
- E₈ Institutional Capital / Total Assets

A = Asset Quality

- A₁ Total Loan Delinquency / Total Loan Portfolio
- A₂ Non-performing Assets in Liquidation / Total Assets
- A₃ Annual Loan Charge-offs / Average Loan Portfolio
- A₄ Accumulated Recoveries from Charged-off Loans/Accumulated Loans Charged-off
- A₅ Non-earning Assets / Total Assets
- A₆ Institutional Capital + Zero Cost Liabilities / Non-earning Assets
- A₇ Financial Stabilization Counterpart (Stabilization Fund)

R = Rates of Return and Cost

- R₁ Total Loan Income / Average Loan Portfolio
- R₂ Total Liquid Cash Investments Income / Average Liquid Cash Investments
- R₃ Total Stock and Bond Investment Income / Average Stock and Bond Investment
- R₄ Total Other Investment Income / Average Other Investment Income
- R₅ Total Interest Cost on Savings Deposits / Average Savings Deposits
- R₆ Total Interest (Dividend) Cost on Shares / Average Shares
- R₇ Total Gross Income Margin / Total Average Assets
- R₈ Total Operational (Overhead) Expenses / Total Average Assets
- R₉ Total Loan Loss Provision Expense / Average Total Assets
- R₁₀ Net Earnings / Average Total Assets

L = Liquidity

- L₁ [Total Liquid Cash Investments - Immediate Obligations] / Savings Deposits
- L₂ Corporate (CFF) Liquidity Reserves / Savings Deposit
- L₃ [Cash on Hand + Checking Accounts] / Total Assets

S = Signs of Growth

S ₁	Growth in Total Assets
S ₂	Growth in Loans
S ₃	Growth in Deposits
S ₄	Growth in Shares
S ₅	Growth in Institutional Capital
S ₆	Growth in Membership

Source: David C. Richardson (WOCCU Advisor).

VI

VILLAGE BANKING PROGRAMS

A. The Original Village Banking Model

The village banking model was first developed during the 1980s in Bolivia by John Hatch, Rupert Scofield, and Aquiles Lanao (Hatch, 1987). Hatch then established the Foundation for International Community Assistance (FINCA) in 1984, to expand the village banking model to the rest of Latin America. With his assistance, other organizations adopted the same or similar models later on. In 1995, village banking was being implemented in at least 28 countries worldwide, including 12 African countries (Nelson *et al.*, 1996). The model has been introduced in several new countries in the past few years.

Village banks are organized by local implementing agencies, which are local partners of international, mostly American, non-government organizations (NGOs) such as Katalysis, Catholic Relief Services (CRS), World Relief, Freedom from Hunger (FFH), Save the Children Fund (SCF), and FINCA International itself. Implementation in developing countries of the village banking methodology by Northern NGOs other than FINCA, and especially in Africa, has gone through numerous adaptations and innovations. In order to better understand the importance and impact of these innovations, it is convenient to start with a review of the original model designed by FINCA.

These changes mean that, in many instances, the original model no longer accurately represents most village banking programs. This learning process has been strong at FINCA itself and at other emulators. Some of these changes have contributed to greater similarities of village banking programs with other West African microfinance organizations.

1. Organizational design

According to the original model, village banking *à la* FINCA works with groups of 30-60 members, usually all women. As soon as the village bank is inaugurated, it receives its first loan from the implementing agency (the local headquarters of FINCA or its affiliate) for on-lending to the individual members of the village bank. The sponsoring agency spends one to three months in setting up each bank, organizing the election of a management committee and training its members, as well as developing the rules and regulations to govern the village bank.

The first individual loan (usually US\$ 50) is repaid on a weekly basis in equal installments of principal and interest over a four-month period. The village bank collects these payments at regular meetings and, at the end of the 16th week, it repays the entire loan principal plus interest to the implementing agency.

The funds circulating back and forth between the implementing agency and the village bank for loans to members constitute the *external account*. If the village bank repays in full, it is eligible for a second loan. If the village bank is unable to pay the amount due, the implementing agency

withholds expansion of further credit until the bank becomes current. Thus, one single borrower in arrears can prevent the entire village bank membership from getting its next loan. To avoid this situation, the village bank's management may opt to draw from the members' savings to cover the loan in default.

This use of savings results in a weak form of *joint liability* among the membership, which creates some incentives for peer monitoring and contract enforcement among village bank members. This structure of incentives is subject, however, to the same kind of advantages and disadvantages of group lending. Peer monitoring constrains opportunistic behavior, but borrowing groups may also experience *domino effects*, thus threatening with generalized default, particularly in the presence of systemic shocks. Because village bank groups tend to be larger than solidarity groups, *free riding* is more likely, and monitoring is correspondingly weaker. Some village banking programs in West Africa have addressed this problem by creating smaller solidarity sub-groups within a village bank.

2. Ownership and governance

The elected management committee makes all investment decisions about the accumulated savings, according to established rules and procedures adopted by the village bank. The committee also oversees and documents all transactions at the village bank. The implementing agency's role in the management of the bank is to support the leadership and facilitate decision-making among the village bank's membership. Agents from the implementing agency attend all weekly meetings initially, but their participation declines as the bank's management capacity grows. The village bank relies on group governance and members of the group remain the owners and residual claimants of the village bank's assets.

3. Financial services

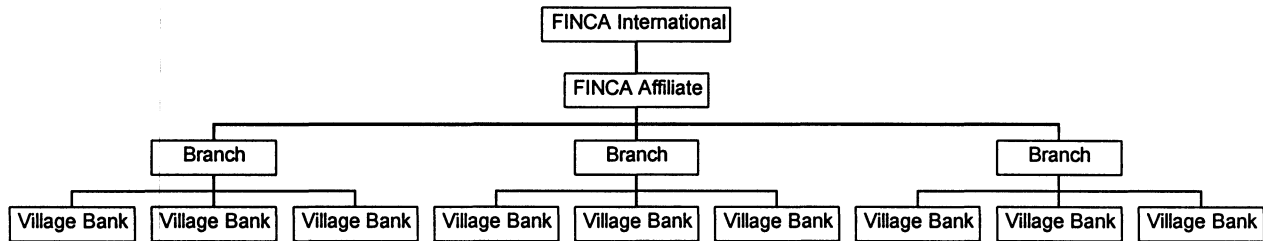
Access to credit at the village bank is linked to savings, and the amount of subsequent loans increases proportionately to the amount of savings mobilized by the village bank from each individual member. In the original model, members were required to save 20 percent of their current loan each cycle. Their next loan can then be as much as their previous loan plus the accumulated savings. Borrowers can receive successive loans until they reach an *external account* loan ceiling of US\$ 300, which occurs usually after approximately three years.

The rigidity of the lending technology, justified by the high costs associated with very small loans, has been a cause of concern among village banking practitioners. They have been seeking ways to develop new products that would introduce more flexibility into this lending technology. The link of savings and loans has been kept, but implementation has become more flexible. Ceilings on loan size have disappeared in many programs.

Member savings plus repayment of principal and interest on the loan with funds from the external account are kept by the bank and constitute the *internal account*. Growth of the internal account follows growth in savings activity. The village bank does not pay any interest on savings but members may receive dividends from internal account earnings. The village bank can in fact use other means to increase internal account funds, such as charging extra interest on member loans from the

Figure 3. FINCA Village Banking Design: Creating NGO Affiliates

FINCA: Creating NGO Affiliates



external account, using member savings for lending activities at rates and terms determined by the membership, making other investments in enterprise or community development activities, and charging fees and fines to members who fail to adhere to its rules.

Member weekly repayments of loan principal are held by the village bank until the end of the loan cycle and can be immediately re-lent from the internal account. Thus, the funds are constantly circulating within the community and the internal account increases while the external account serves to stimulate internal account activity. The designers of the FINCA village banking model estimated that, at the end of three years, the *internal account* funds would be sufficient to meet all members' demand, resulting in *graduation* of the village bank. At that point, the implementing agency would withdraw its funds and use them to start a new village bank. Graduation results, however, in an adverse structure of incentives. It implies the lack of permanency of the relationship with the external source of funds, thereby reducing incentives to repay as graduation time approaches. For this reason, many programs have not implemented the graduation rule.

4. Evolution of the model

Key features of the original village banking model are standardization, collective liability, and credit linked to savings. Lending policies and products are tailored not to meet individual demand but to attract the poorest, especially women. This village banking model has been subject to several transformations, to respond to member's demand and to adapt it to local circumstances, as is the case with the programs visited for this case study in West Africa. Changes made to the original model include the revision of loan policies, addition of non-financial services, changes in external and internal account practices, and abandonment of graduation.

In effect, some of the changes have contributed to making these village banking programs share several similarities with other West African microfinance organizations such as the *caisses villageoises*. Graduation, for example, has been a major issue in the West African village banking programs. The implementing agencies have not been willing to withdraw their funds at the end of the cycle at all, allowing the program to continue operating with each village bank beyond the originally proposed three years. At the FFH program in Mali, graduation for a village bank member means being able to afford individual membership into the Kafo Jiginew, the partner credit union.

Table 14. Village Banking Methodology Compared: The Standard Model versus Adaptations in West Africa.

Methodology	Standard FINCA Model	Adaptations
1. Organization		
Membership	30-50 members	16-432 members
Structure	Single group	Solidarity groups of 3-8 within the village bank
Gender	Targeted exclusively to women	Men and women
2. External Account		
Use of loan funds	Trading	Trade, microenterprise, agriculture
First-cycle loan maximum	US\$ 50	US\$ 50
Loan ceiling	US\$ 300	US\$ 300 and upwards
Interest	To cover operating costs	Positive real rate of interest
Term of the loan cycle	16 weeks	16-24 weeks
Repayment Schedule	Equal weekly installments of principal, interest, and savings	Weekly, bi-weekly, monthly
3. Internal Account		
Use	Individual and group enterprises	Deposit in bank account, loans to others, group enterprises
Savings	Forced savings, 20 percent of loan amount, tied to new loan size, restricted access for village capitalization	Forced savings, voluntary savings, minimum amount required, formal bank deposits, withdrawal policies, not necessarily tied to loans
Control and monitoring	Members	Implementing agency (CRS, FFH, SCF), partner financial institution, and members, MIS system, formal bank account
Lending	100 percent lent	
4. Graduation	After 9 cycles and US\$ 300 limit reached. Village bank becomes self-capitalized, self-managed	Remain clients of program, higher loan levels, become client of partner financial organizations

Sources: Seep Network and OSU field visits.

Loan ceilings have been revisited as have also been the frequency of loan repayments and the mechanisms to increase loan amounts (see Table 14). This case study reviews the performance of several programs that have included these transformations in their operations. The sections below analyze the programs run in West Africa by three US-based NGOs, namely, Freedom from Hunger (FFH) and Save the Children Foundation (SCF) in Mali and the Catholic Relief Services (CRS) program in Benin.

B. Freedom From Hunger and the Kafo Jiginew's Village Banking Program

B.1 Kafo Jiginew Credit Union Network

Freedom from Hunger initiated its village banking methodology, *Credit with Education*, in 1989. All village banking programs sponsored by FFH are carried out through partnerships with local microfinance organizations, including credit unions (CUs). The first experiment of a village banking program implemented through a credit union network in Africa was started in Burkina Faso in 1993 with the *Réseau des Caisses Populaires du Burkina Faso* (RCPB). As of June 1997, the RCPB was reaching 18,113 members, over 12,000 of whom had an outstanding loan. The program expanded later on to FUCEC-Togo, the Togolese credit union network. In Mali, FFH has been working with two CU networks since 1996. They are the Kafo Jiginew and Nyesigiso. The Kafo Jiginew program operates in the region of Koutiala, and it is reviewed for this case study.

Credit with Education is a strategy that combines village banking with low-cost, non-formal education, to assist women to build their productive assets, accumulate savings, acquire self-confidence, and improve basic business and family survival (health, child survival, and nutrition) skills (Stack, 1997). The ultimate objective is to improve nutrition and food security for the most vulnerable groups among the poor.

Since 1989, FFH has focused on developing and adapting this strategy in eight countries. Nine of FFH's 14 local partners are financial institutions, and four of them are credit union networks. This case study focuses on the financial dimensions of the FFH strategy, and it ignores important non-financial impacts (MkNelly, 1997). Issues related to the advantages and disadvantages of combining financial and non-financial services are also ignored.

1. Organizational design

The Kafo Jiginew is a network of credit unions located in Koutiala, a cotton-producing region in Southern Mali. Jiginew means granary in the Bambara language. Kafo Jiginew means the union of all granaries, and it was created as a federation in 1988, by the union of five credit unions, with help of a consortium of several international donors from Italy, Belgium, Germany, and the French Credit Cooperative Federation (*Consortium Européen pour le Crédit Coopératif Malien*). Until 1994, technical assistance for the credit unions was provided by the French.

Koutiala was chosen because it is a relatively rich area, due to the cotton growing activities. The Kafo Jiginew is now fully owned and managed by Malian members, staff, and board. The higher literacy rate of the population was also a favorable factor in this choice. The credit unions needed a potential membership of people with relatively stable and continuous income flows. The vast majority of the population lives in villages in the rural areas.

A credit union or Jiginew is created only where CMDT, Mali's Cotton Marketing Board, operates. A Jiginew usually belongs to several villages, ten on average, which in turn are part of a ZAER, *i.e.*, a grouping of villages determined by CMDT for cotton marketing purposes. A ZAER covers a radius of 15-20 kms. The choice of the village to house the credit union is made during a general assembly of potential members and the federation.

All construction materials and expenses for an office are the responsibility of the villagers. After the physical structure is in place, the new credit union receives furniture, other office materials and free technical assistance for three years from the federation, *i.e.*, the Kafo Jiginew. After that period, fees for all services are gradually charged to the credit union.

As of December 31, 1997, Kafo Jiginew had a network of 76 credit unions and 11 regional unions in three regions: Koutiala, Sikasso, and Fana. The Kafo Jiginew, the federation, is a central financing facility as well as provider of technical assistance for member credit unions.

The system follows the standard COOPEC (*Coopératives d'Epargne et de Crédit*) structure, according to which members are both clients and owners. This management structure consists of three levels: the governance structure of each credit union, regional unions of 8-10 credit unions, and the Kafo Jiginew.

Each credit union is run by two managers, a board of directors, a credit committee, and a supervisory committee, all elected at the annual general assembly meeting. The board of directors is made up of 12-15 members from all villages that belong to the credit union, to assure a fair participation by all. At least one person from each participating village is selected. Members of the board of directors are the president, vice-president, secretary general, vice secretary general, treasurer, vice treasurer, credit officer, comptroller, conflict officer, and several organizers.

The board of directors is also the executive body of the organization, and it sets the agenda for the general assembly of members. Members of the board of directors meet on a monthly basis. The board selects two cashiers among villagers to manage the cash flow in the credit union. A credit committee, which reviews all loan applications, and a supervisory committee are formed by members of the board of directors.

The credit committee is made up of four members, of whom three are permanent. Having one non-permanent member allows the credit union to give the opportunity to other members to join the credit committee at some point. Members have to be from different villages to minimize any bias and favoritism. The supervisory body has two to three members, and it is the control body of the credit union. Members of both boards are elected for three years and can be reelected indefinitely. Only one-third of the officials can be replaced during an election each year.

Manager salaries depend on the profits made by the credit union but cannot exceed CFAF 500,000 (US\$ 1,000) per year. Income generated from photograph fees paid by members when registering are used to pay managers an additional per-diem for food and gas on the days the credit union opens. Managers of urban credit unions receive a monthly salary of at least CFAF 20,000 (US\$ 40). At the time of the case study, the average monthly salary in all three urban credit unions was CFAF 35,000 (US\$ 70), which is slightly higher than the minimum wage in Mali.

Fee income is also used to compensate board members, who receive a per-diem every time they meet. After five years, the board of directors receive CFAF 1,500 (US\$ 3) for every auditing function they perform. These incentive schemes that tie compensation to results of the organization are important to motivate managers, who are responsible for the day-to-day operations of the credit union

although overall control of the organization rests with board members. Performance-based compensation makes the incentives of the managers compatible with the interests of the organization.

Regional unions meet regularly to discuss issues of common interest. The Kafo Jiginew, the federation, is a central financing facility for all member credit unions. It intermediates funds between deficit and surplus units. Surplus units can retain from CFAF 500,000 to CFAF 1 million (US\$ 1,000 - 2,000) in their local organizations for loans in periods of low loan activity and up to CFAF 10 million (US\$ 20,000) during high loan granting periods such as the month of June. The federation manages the liquidity of the entire network as a single entity. There is no intermediary structure between the federation and local credit unions. It also provides training to the board, cashiers, and committee members of the CUs.

2. Policies

The Kafo Jiginew is supervised by the West African Central Bank (BCEAO) and by the Malian Ministry of Finance under the PARMEC law.

Kafo Jiginew credit unions open once to twice a week. They mobilize their own savings to grant loans to members. People from different villages can belong to the same credit union. To become a member and have access to loans, a membership fee of CFAF 5,000 (US \$ 10) is required and may be paid in four installments to accommodate the poorest. Women can have access to a loan after paying just CFAF 1,000 (US \$ 2) for their membership fee. They are expected to eventually complete payment of the fee in the future. A minimum savings of CFAF 5,000 (the initial share payment) gives access to a CFAF 50,000 (US \$ 100) loan. Credit amounts are thus linked to savings.

Deposit products include current accounts, which require a minimum of CFAF 1,000 and pay 3-4 percent annual interest, compounded quarterly. Term deposit accounts have a minimum balance requirement of CFAF 25,000 (US \$ 50) to be kept for at least a year and pay 4-6.5 percent annual interest. This rate is only slightly higher (one point difference) than those offered by commercial banks. They are much lower than the rates paid by the *caisses villageoises* on deposits.

The loan portfolio is funded by member shares, term deposit accounts, and 50 percent of current accounts. In recent years, outside funds borrowed from BNDA, the Agricultural Development Bank, have been used to complement deposit funds and have also allowed the credit unions to grant larger and longer-term loans. Several loan products are offered by the credit unions at different rates of interest to reflect the term to maturity of the loans. Longer-term loans carry lower interest rates. Loan products are:

- (a) short-term, small loans granted for three months at 4 percent monthly interest,
- (b) agricultural loans granted for eight to ten months at 2 percent per month,
- (c) equipment loans granted for two to three years at 1.2 percent per month, and
- (d) *credit with education* (FFH village bank loans) granted for 16 weeks at 3 percent per month.

Short-term, small loans are for social and emergency purposes and do not require the approval of the entire credit committee. The decision can be taken by the president alone. Agricultural loans

are disbursed every year in June and July, to allow farmers time to buy seed for the coming planting season. Equipment loans are granted to buy carts and farm animals. Some small loans are also granted to young microentrepreneurs in urban areas. There is high seasonality in loan granting and repayments at the credit unions for the most popular loan product, *i.e.*, agricultural loans. In fact, most farmers are engaged in the same agricultural activity, *i.e.*, cotton growing and a bad year in cotton may disrupt credit union activities. This reflects the obstacles to financial intermediation in a risky environment.

3. Lending technologies

Kafo Jiginew credit unions grant loans mainly to individuals but also to some groups. Credit is tied to savings and individual members can obtain loan amounts up to ten times their savings balances. The ratio, considerably higher than the traditional 2:1 for credit unions, allows members in practice to only get loans up to a maximum determined by individual credit unions. Collateral requirements for loans include physical assets such as land, agricultural and other equipment, a co-signor, or a village association.

It is worth noting that the credit unions were first created and membership gathered through *associations villageoises* (AVs), village groups formed for the marketing of cotton. Thus, the majority of male credit union members are also AV members, through which they sell and receive income for their products. Thus, the use of village arrangements, an important factor in the early life of the credit unions, continues to play a key role in contract enforcement and thereby the performance of the organizations. In an effort to boost the female membership of the credit unions, Kafo Jiginew welcomed the opportunity to add a village banking *credit with education* program to its activities in 1995.

B.2 Freedom From Hunger's *Credit with Education* Program

The Freedom from Hunger *credit with education* program is primarily designed to improve nutrition and food security for poorer women and their children. Women attend education classes once a week for four weeks before any loan activity, which then starts on the fifth week. Working in partnership with credit unions offers several advantages to this village banking program:

- (a) credit unions have a social agenda (which suits FFH) in addition to providing financial services,
- (b) credit unions mobilize their own funds (deposits) for loan purposes,
- (c) credit unions usually have a large and widespread network of member organizations,
- (d) credit unions are eager to attract new members, especially women,
- (e) credit unions are run on cooperative principles, which coincides with village banking principles, and
- (f) credit unions value peer recognition and approval.

By using credit unions, FFH is able to implement its village banking program within a well-structured microfinance organization and to achieve outreach fairly quickly by having access to the large network of credit unions in poorer areas of the country. Member credit unions readily accept

the partnership because it allows them to attract more members and especially increase their pool of women members. Village banking offers them an opportunity to lend to poorer members.

Credit unions treat village bank women groups as any other group member such as the AVs. Each group is treated as an individual member of the CU. The women guarantee repayment of each other's loan at both the solidarity group and the credit association levels. Thus, the Kafo Jiginew did not have to add a group technology to their regular individual savings and loan technology to accommodate the FFH village banking program. It has been a fruitful symbiosis.

1. Policies

Under the village banking program at the Kafo Jiginew, groups of women form *credit associations* (CAs) of 16 to 36 members made up of *solidarity groups* of 4 to 6 women. Credit associations register as members of the local credit union and receive their first loan for four months. As of December 1996, there were 264 CAs which were members of 15 local Kafo Jiginew CUs.

2. Technologies

Credit unions use their own funds to lend to village-bank members. Women go through a training program that lasts four weeks before they receive their first loan. The program, which started in August 1995, is run by 15 *animatrices* (coordinators) paid by FFH. During the training period they meet the coordinator every week and save CFAF 100 (US\$ 0.2) to CFAF 500 (US\$ 1.0) per week per woman to constitute the group fund and accumulate the required membership fee of CFAF 10,750 (US\$ 21.5) for a group of 30 women to open an account at the Kafo Jiginew. Each woman pays CFAF 350 (US \$ 0.7) as membership fee. There are also additional fees for photos.

During the four-month loan period, forced savings of CFAF 100 per week go into the internal account. The minimum first loan is CFAF 2500 (US\$ 5) and the maximum first loan is CFAF 25,000 (US\$ 50). There is also a maximum loan ceiling of CFAF 150,000 (US\$ 300), which is reached after about 11 loan cycles of four months each. For the first three cycles, 1/15 of the loan amount is reimbursed every week. Loan repayment is due every week during the first three loan cycles, then every two weeks until the sixth cycle, and monthly repayment starts with the seventh cycle.

The nominal interest rate on the loans is 13-16 percent per cycle depending on the credit union (12 percent for the program and 1-4 percent for the village bank association). The average inflation rate was 5.8 percent per year in Mali in the period 1990-1997, so these rates are positive in real terms. There is also contribution to a guarantee fund required by the Kafo Jiginew equal to 5 percent of the loan amount.

The internal account is made up of loan repayments, plus forced savings (CFAF 100 per week), plus voluntary savings, plus the group fund. The group fund is made up of leftover voluntary savings accumulated to pay the membership fee at Kafo Jiginew, plus penalties levied on village bank members for missing or being late at meetings, plus occasional grants, plus interest on loans. This internal account earns 3 percent annual interest in a savings account at the Kafo Jiginew. Group funds can be

used for group projects or can be partly used to pay membership fees at the Kafo to open individual account for village banks members chosen by their peers.

Women are allowed to take different loan amounts within the group. At the end of every loan cycle, members are allowed to withdraw their savings and usually do so. Loan sizes increase by CFAF 12,500 every new cycle. FFH intended loan sizes to increase by 50 percent every new cycle, but village banking management at the Kafo Jiginew was applying a different rule for fear of too rapid growth in loan sizes from one cycle to another. Thus, if the first loan is CFAF 25,000, the second loan will be CFAF 37,500 (25,000+12500), and the third loan will be CFAF 50,000 (37,500+12,500).

As of December 1997, the oldest of the 264 existing associations were in their 6th cycle. By the time the associations reach their 11th loan cycle and CFAF 150,000 (US \$ 300) in loans, it is hoped that the women will have accumulated enough savings to “graduate” to the Kafo Jiginew, by opening individual membership accounts at the credit union and enjoying additional financial services reserved to full-fledged individual members. In fact, village bank members have already rewarded some of their members with an individual account at the Kafo Jiginew, paid for by the group fund. These new Kafo members can remain as village bank members to take advantage of the education program.

3. Outreach

As of September 1997, there were 6,736 village bank members in 264 credit associations at 13 Kafo Jiginew credit unions. There were 12 to 22 credit associations per credit union. Members in the associations represented 15 percent of total Kafo Jiginew membership, of whom only 8 percent are female. Total loans outstanding were CFAF 136,788,000 (US\$ 273,576) granted to 5,859 active borrowers. The total amount of deposits was CFAF 8,920,460 (US\$ 17,841).

Village bank member loans are not funded by bank member deposits but from Kafo Jiginew funds which include deposits as well as outside funds from the BNDA. The highest loan amount at that time was registered at the oldest associations, which were at their sixth loan cycle. This implies that each member had a loan of CFAF 87,500 (US \$ 175). The FFH village banks cater mostly to women and the poor in general, who start with loan sizes of CFAF 25,000 (US \$ 50) or less.

4. Sustainability

The FFH village banking program with the Kafo Jiginew had a repayment rate of 100 percent compared to 95 percent for the credit union network itself. The design chosen by FFH to work with the Kafo Jiginew gives a whole new perspective to the survival of its village banking program, since its long-term viability is intimately linked to the sustainability of the partner credit unions. Thus, the sustainability of the credit associations is highly dependent on the sustainability of the partner credit union. Credit associations are also (group) members of the Kafo. In contrast with the original FINCA village bank model, which relies entirely on outside funding for on-lending, FFH has chosen a clear path to sustainability by integrating its associations into well-structured and performing financial organizations.

Table 15. Indicators of Outreach of the FFH Village Banking Program with the Kafo Jiginew in Mali, 1997.

	September 30, 1997
Number of credit associations	264
Number of village bank program staff members	25
Number of association members	6,736
Number of outstanding borrowers	5,859
Outstanding loan balances (CFAF)	136,788,000
Outstanding savings (CFAF)	8,920,460

Source: Freedom From Hunger and Kafo Jiginew files.

5. Operational self-sufficiency

The organization's operating costs as a percentage of its average loan portfolio reveal how much it costs to lend one CFAF. In the case of the Kafo Jiginew, operational expenses were 14.5 percent on average over the two-year period of 1995 and 1996 (Table 15). In 1996, CFAF 0.17 was spent for every CFAF 1 lent. The Kafo Jiginew credit unions are able to run a reasonably efficient operation for this type of clientele, keeping operating costs at a low proportion of their loan portfolio.

Operational self-sufficiency, defined as the ability of these organizations to cover their operating costs with revenues, had not been yet achieved. At the Kafo Jiginew credit unions this proportion was 90 percent on average (Table 16). The credit unions were able to cover close to 90 percent of their operational costs with their revenues. Thus, the Kafo Jiginew credit unions, though not operationally self-sufficient, were very close to achieving this goal. Operations at the credit unions are becoming increasingly self-sustaining.

Average return on assets (ROA) increased from 4.7 percent in 1995 to 7.7 percent in 1996. Average return on equity (ROE) also increased from 19.4 percent in 1995 to 35.8 percent in 1996 (Table 16). These ratios suggest that the Kafo Jiginew credit unions are performing above industry standards. These ratios overestimate the profitability of the Kafo Jiginew credit unions, however, because they include a strong positive impact of donor grants, such as those from FFH, on program revenues and equity. If the preceding years are any indication of the future, nevertheless, aggregate profitability of the Kafo Jiginew credit unions is expected to increase in the years to come.

Table 16. Financial Indicators and Operational Efficiency at the Kafo Jiginew, 1995-96.

	Sept-30-95	Dec-31-1996
Financial expenses	27,195,782	56,954,875
Operating expenses ^a	160,067,343	296,264,341
Total expenses	187,263,125	353,219,216
Financial income ^b	186,947,314	326,163,668
Other income	80,698,644	223,198,527
Total income	267,645,958	549,362,195
Net income	80,382,833	196,142,979
Financial assets	1,687,315,008	3,132,412,704
Average total assets	1,708,362,276	2,536,643,305
Average total equity	414,387,983	548,303,394
Total liabilities	1,708,362,276	3,364,924,333
Average outstanding portfolio	1,356,158,497	1,713,373,508
Operating expenses/average outstanding portfolio (%)	11.8	17.3
Operational self-sufficiency ^c	91.3	89.9
ROA ^d	4.7	7.7
ROE ^e	19.4	35.8
Gross financial margin ^f	9.4	10.6
Net operating margin ^g	0.0	-1.1

Source: Kafo Jiginew reports.
All amounts in CFAF.

Notes: *a*: Operating expenses are equal to personnel expenses and administrative expenses, including depreciation of fixed assets. They do not include financial costs and loan loss provisions.

b: Financial income = income from interest and loan fees.

c: Operational self-sufficiency = Financial income / Financial costs + Operating costs + Loan loss provision.

d: ROA = Net income / Average total assets.

e: ROE = Net income / Average total equity.

f: Gross Financial Margin = (Financial income - Financial costs) / Average total assets.

g: Net Operating Margin = Gross financial margin - Operating costs / Average total assets.

6. Financial self-sufficiency

The sustainability of the Kafo Jiginew credit unions depends on their financial self-sufficiency, *i.e.*, their ability to generate sufficient income to cover not only operating costs but financial costs as well. The net operating margin for the Kafo Jiginew was -1.1 percent in 1996 (Table 16). A negative net operating margin reveals that the Kafo Jiginew credit unions are not covering their total costs with income derived from their loan operations. In fact, the credit unions receive grant money from donors such as FFH for their operations, but not for on-lending purposes.

7. Ownership and governance

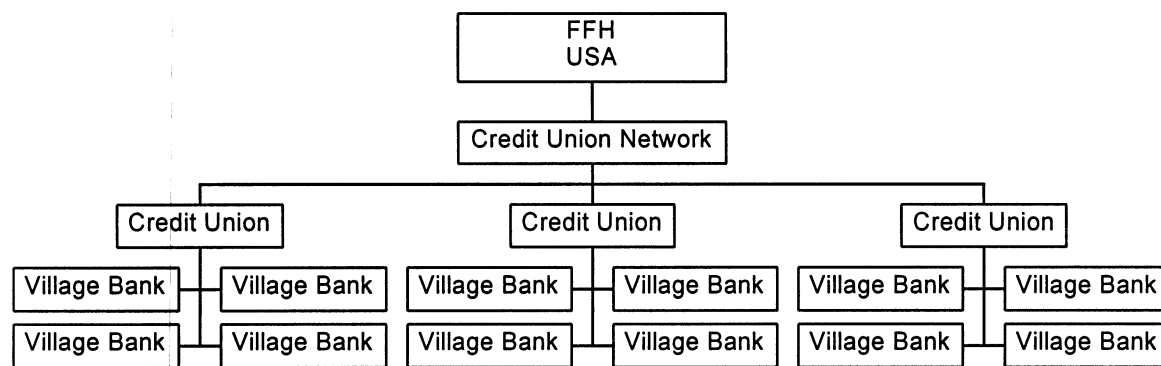
The FFH village banking program at the Kafo Jiginew is managed by a staff made up of a director and 15 *animatrices* or coordinators hired and remunerated by FFH. Each *animatrice* is responsible for several credit associations. The elected management committee at each association is comprised of a president, secretary, treasurer, comptroller, information and organization counselor, and an education counselor. The management committee also oversees and documents all transactions at the village bank. The *animatrice* attends all weekly meetings, which include education sessions on health and nutrition, and supervises loan repayment.

The credit association members rely on group governance and peer pressure to ensure prompt loan repayment. However, the association itself is a member of the local Kafo Jiginew credit union, from which it gets its loan funds. Thus, credit members should have the same claims on credit union assets as other members (Stack, 1997). The Kafo Jiginew is subject to the same diluted ownership structure that exists in any credit union. This structure carries with it the conflicts of interests of the dual role of client and owner.

So far, these conflicts have been minimized by active deposit mobilization, but they will increase with growing access to external funds, which create the threat of borrower domination. Furthermore, the rule of one person, one vote may constrain the growth of deposits. In turn, the village banks themselves are subject to the shortcomings and advantages of group rather than individual credit.

Figure 4. FFH Village Banking Design within the Credit Union Framework.

FFH: Working with Credit Unions



C. Save the Children Foundation

1. Organizational design

Save the Children Foundation (SCF) started its integrated development approach in Kolondieba, Mali in 1988. The program included water, health, and credit services for the target population. The first SCF village banking program started in 1991 in 15 villages where a *Communauté Villageoise de Développement* (CVD) was created as a channel to disburse agricultural loans to members. The CVDs were transformed later on into *associations villageoises* (AVs), concerned with all development aspects of the village, not just financial services.

The AV organizational structure included three units, one each in agriculture, health, and credit. The AVs received a grant of CFAF 29 million (US \$ 50,000) to offer loans for agricultural inputs to the villagers. Some loans were granted for three to four years, even during the early stages of the program. Later, the credit unit at the AV was transformed into a specialized financial organization or COVEC (*Coopérative Villageoise d'Epargne et de Crédit*).

In the meantime, from 1988 to 1991, the AV members were trained in the management of financial services to prepare them for transformation into COVEC units, which were to be run like credit unions. Thus, each COVEC was organized around a general assembly, a management committee, a credit committee, and a supervisory body. Members of a COVEC pay CFAF 1,050 (US \$ 2.1) as a fee, and CFAF 1,000 (US \$ 2) buys the member a share. Loans are granted principally to buy agricultural inputs or cereals and for microenterprises. Forced savings of 10 percent of the loan amount are required of every borrower.

All COVECs then formed the *Union des Coopératives Villageoises d'Epargne et de Crédit* (UCOVEC) in 1991, in which the original 15 villages were included. When the number of COVECs grew from 15 to 43 villages, UCOVEC formalized its existence by becoming Faso Jigi, the federation of all COVECs, which remains the only legally recognized entity of the network. A total of 1,493 people had received loans from the 43 COVECs as of December 31, 1996. The repayment rate was only 36 percent of amounts due. In view of this low repayment performance, the program was being revised. All COVECs were to be closed, leaving Faso Jigi to act as the only credit union for the whole Kolondieba district. If the experience proved successful, other credit unions were to be opened in municipalities and later on in villages.

It was against this background that the SCF introduced its village banking program, called the Group Guarantee Lending and Savings (GGLS) Program. The program started in March 1995, in an effort to boost female membership in Faso Jigi. The GGLS started, with USAID funding, in five villages of the Kolondieba district and with CFAF 12.5 million (US\$ 25,000).

The GGLS program is being run by 15 SCF staff members in Kolondieba, including eight coordinators responsible for several GGLS units. Each GGLS unit is comprised of three solidarity groups of six women each, for a total of 18 people per GGLS unit. The women know each other well. They choose five members to form the executive committee, made up of a president, secretary, treasurer, and two other officers.

As of December 31, 1997, there were 34 GGLS units in as many villages in the Kolondieba district. While some GGLS units were members of the local COVEC, others were stand alone groups (see Figure 5). The total membership was 2,580 women, who were involved in diverse economic activities such as petty trade and microenterprises.

2. Policies

Funds for the GGLS program come from SCF, even for those GGLS units that are members of local COVECs. The first loan to a GGLS unit is between CFAF 5,000 and CFAF 25,000 (US\$ 10 - 50), for a period of four to six months. The term to maturity is four months in towns and six months in villages. The solidarity groups that form a GGLS unit can demand different loan amounts not to exceed the maximum for the cycle. Members of each solidarity group of six women receive, however, the same loan amount.

The annual nominal interest rate charged on loans is 28 percent. Repayment is due every week. An additional 5-percent application fee is charged per loan, and members are required forced savings of 5 percent of the loan amount. Therefore, the effective annual interest rate on loans was 37.5 percent. In real terms, the rate was 31 percent in 1997. After a year into the program, due to numerous complaints from members, repayment schedules were changed and payments were required twice a month. Loan sizes increase 10 percent from one cycle to the next and, at the end of each cycle, women are allowed to withdraw part or all of their accumulated savings. The oldest GGLS units are at their seventh loan cycle, with a six to eight month terms and an average loan size of CFAF 37,500 (US\$ 75).

3. Lending technologies

Several solidarity groups made up of six women each form a GGLS unit. In Kolondieba-ville, one unit was made up of 72 solidarity groups of six women each, for a total of 432 GGLS members. Each village bank member pays a one-time membership fee of CFAF 100 (US \$ 0.5). The three elected executive officers of the GGLS (president, treasurer, and secretary) are in charge of reviewing loan applications for submission to SCF.

Solidarity group members are granted the same loan amount each. This amount may differ throughout the GGLS from one solidarity group to another. Groups are thus allowed to take different loan amounts. In fact, in one of the villages visited, some members were still demanding CFAF 25,000 (US \$ 50) after the fifth loan cycle. Group liability serves as collateral for all loans. In case of default, other GGLS members would repay the loan and expect to be paid later. If a member behaves in a fashion that is not appreciated by other group members, she can be asked to leave the group. GGLS members meet every time a loan payment is due (once a week) and at the beginning of each loan cycle, when new loans are granted.

4. Outreach

GGLS units provide small loans largely to poor women in rural and urban areas. The average loan size as of September 30, 1997 was US \$ 50 at the time of disbursement. As of that date, the program had a loan portfolio of CFAF 25,041,000 (US\$ 50,082) with 2,178 loans outstanding (see Table 17). These clients appear to be poorer than those of other programs in this case study.

The number of women borrowers grew from 780 in September 1995 to 2,378 in September 1997, *i.e.*, a 221 percent increase. The outstanding loan portfolio increased 65 percent and savings increased 55 percent from December 1996 to September 1997. These are forced deposits equivalent to 5 percent of the loan amount, however, withdrawable at the end of the loan cycle. There were no *voluntary* savings in the program. The long-term objective of the program is to reach 4,500 women in 75 villages in Kolondieba district. The breadth of outreach of this program is therefore not as significant as in the other cases.

5. Sustainability

The repayment rate at the GGLS program was 100 percent of outstanding loans as of September 1997. The program, however, is not sustainable. The operational self-sufficiency ratio was only 27 percent and the financial self-sufficiency ratio was 25 percent (see Table 17). That is, program revenues covered only about one-quarter of all program costs. The program hopes to achieve 86 percent sustainability after five years, *i.e.*, by the year 2000.

Table 17. Indicators of Outreach and Measures of Performance for the GGLS Program in Mali, 1996-97

A. Program Characteristics	Dec. 31, 1996	Sept. 30, 1997
Number of loans outstanding	2,178	2,472
Volume of loans outstanding (CFAF)	25,041,000	26,206,000
Number of compulsory savings accounts	764	2,472
Proportion of female clients (%)	100	100
Staff members	17	17
Nominal annual interest rate on loans (%)	28.0	28.0
Effective annual loan interest rate (%)	37.5	37.5
Real annual loan interest rate (%)	31.0	31.0
B. Performance Measures		
Operational self-sufficiency (%)	--	27.2
Financial self-sufficiency (%)	--	25.0
Number of active loans/staff	--	155
Average loan size (CFAF)	--	24

Source: GGLS files.

For the future of the GGLS program, Save the Children is training local women or *jurumuso*, who would assist the SCF staff monitor GGLS activities, including loan repayments. Another element in the exit plan of SCF is to rely on Faso Jigi, the credit union, for the provision of future funds for the program. The SCF will continue to provide technical assistance, supervision, and some funding. Faso Jigi be a legally recognized credit union, and it can continue to attract funds from the commercial banking sector, particularly from the BNDA, the Malian Development Bank. Faso Jigi was successful in borrowing twice from BNDA in 1995 and 1996. BNDA lent to Faso Jigi at 10 percent annual interest rates for nine months. Faso Jigi lent that money to its member-COVEC at 11 percent annual interest and the ultimate borrowers were granted loans at 17 percent annual interest.

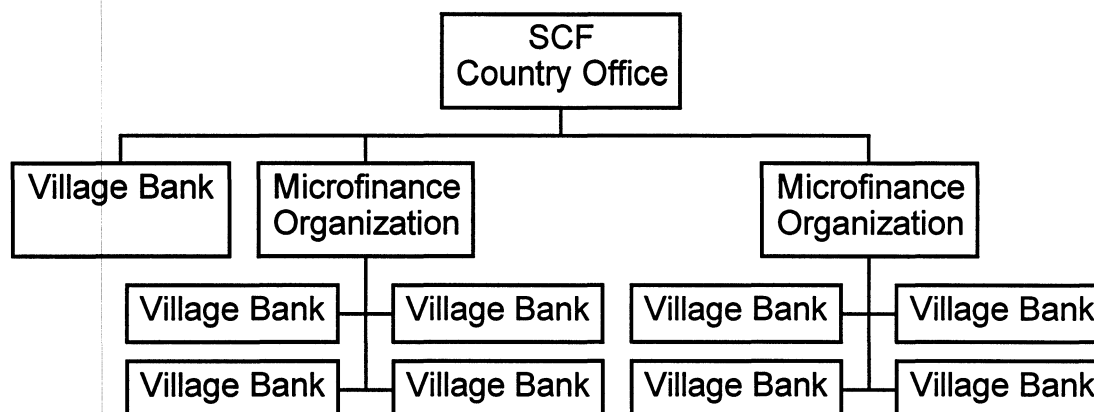
Thus, the future of GGLS is tied to the performance and sustainability of Faso Jigi. The arrangement of having the GGLS women linked to a well-functioning microfinance organization is better than operating as stand-alone groups, whose future would be far less certain. Many issues must be resolved, nevertheless, for this program to become sustainable.

6. Ownership and governance

The GGLS units rely on group governance. Members of the group are the owners and residual claimants of the village bank's assets. The common future of Faso Jigi and the GGLS units calls for an executive management committee to represent all 34 GGLS units at the Faso Jigi's management level. Thus, the GGLS units will become members of Faso Jigi and would be entitled to one vote as other individual shareholders as well as to all other membership rights that a credit union member is entitled to.

Again, all issues concerning the stability of borrowing groups are relevant for the GGLS units. Moreover, the shortcomings of property and governance structures of CUs will also influence the opportunities for success of this experiment. Linking the village banks to a credit union is a good idea, as the FFH experience in Mali illustrates, but it is not sufficient. Strong management skills and sustained technical assistance are also needed. Aspiration to large-scale operations are also important to address economies of scale issues and to evolve into a more complete organization.

Figure 5. SCF Village Banking Partnership with Local Microfinance Organizations
SCF: Partnership with Local Microfinance Organizations and Direct Implementation



D. Catholic Relief Services

1. Organizational design

Catholic Relief Services (CRS) operates village banking programs in several African countries, including Benin, Burkina Faso, Ghana, Senegal, and Uganda. CRS usually operates through local NGOs, which may be involved in other activities besides microfinance. The organization provides start up funding and technical assistance to local partners but also expects them to develop into autonomous microfinance organizations. The amount of resources devoted to capacity building of the partner NGOs may be substantial. This is a long-term endeavor, especially when the NGOs do not specialize in microfinance.

CRS started its village banking program in Benin in 1992 in partnership with CREDESA, a local NGO which specializes in health-related activities. CREDESA (*Centre Régional pour le Développement et la Santé*) was created in 1983 to provide health services to the rural population. It is also involved in research and training. The village banking program mixes credit with some education on health issues and literacy, which are compulsory programs that the village bank members must attend.

The village banking program started with six banks, and it expanded in 1994 to two other local NGOs. These are the *Groupe de Recherche et d'Action pour la Promotion de l'Agriculture et du Développement* (GRAPAD), in the Mono region, and the *Centre de Recherche des Idées de Développement Agricole et Artisanale* (CERIDAA), in the Oueme region. By December 1997, CRS was running a total of 59 village banks through CREDESA (24 banks), GRAPAD (19 banks), and CERIDAA (16 banks). CERIDAA operated another eight village banks sponsored by Oxfam, an international NGO.

2. Policies

CRS provides the initial fund to start the village banks as well as ongoing technical assistance to the partner NGOs. The fund is allocated as loans to village bank members and, when repaid, it constitutes the *external account* for the program. The local NGO receives additional complementary funds from CRS at every new loan cycle, to grant increased loan amounts to members until the maximum loan limit is reached.

Village banks are formed by a group of 50 women, who form solidarity groups of 3-8 people. This is the same mechanism used by other Malian programs to deal with the large number of members in the village bank. This, in turn, reflects that there is only one village bank at each location. Each solidarity group is run by a credit chief. The management committee at the village bank level is made up of five members (president, secretary, treasurer, and cashier), who are all solidarity group chiefs.

The maximum first loan amount is CFAF 25,000 (\$50). Forced savings of at least 20 percent of the loan amount are required. Each loan cycle is six months long. The interest rate on loans is 15 percent per cycle (2.5 percent per month), of which 10 percent is kept by the NGO, 3 percent is kept in the *internal account* of the village bank, and 2 percent is designed to account for inflation. The effective cost of a loan to borrowers is raised substantially due to the requirement of forced savings. Loans are repaid on a monthly basis and consist of 1/6 of the interest, 1/6 of the principal, and 1/6 of the forced savings due. The amount of the loan in the next cycle is obtained by adding the accumulated savings to the previous loan amount.

A voluntary savings deposit of CFAF 200 to CFAF 500 allows the village bank to open an internal account for a member. Savings are still not being remunerated by the village banks, although this is highly encouraged by CRS. This will not be likely to happen, however, with such an important element of forced savings still in place. The village bank's internal account is made up of interest earned on loans, forced and voluntary savings, and other revenues from penalties levied on members for diverse reasons. Village bank members cannot withdraw their accumulated forced-savings before the end of the program. They can, nevertheless, withdraw their voluntary deposits, if any are available. Funds from the internal account are used in some village banks to grant loans at a higher interest rate (18 - 25 percent) and at shorter terms to maturity than six months, to non-members. These loans are repaid in a monthly basis.

The maximum loan amount in a village bank is CFAF 100,000 (\$200), to conform to the desire to cater to the poor, according to CRS. This ceiling is reached in the 6th loan cycle, after roughly three years, if village bank members take up the maximum loan size permitted at each cycle. Village bank members are allowed to take less than the maximum loan amount available each cycle.

The CRS originally anticipated the village bank to become self-sufficient at that point and to be able to rely on its savings and internal account to continue its operations. Village bank members would each have accumulated CFAF 70, 000 (\$140) in savings. However, in the field things did not operate as planned. The oldest village banks have already reached their eighth cycle and are still not self-sufficient. CRS has no plan to pull out its funds from the program. One lesson learned from this field experience is that six cycles are too short for the village bank to achieve self-sufficiency, if ever.

The accumulated savings by that time are still low and less than the amount of the last loan received by the members (CFAF 100,000). Thus, the belief at the local CRS office in Cotonou is that members should be allowed to continue their village banking activities as long as they wish.

An example of the loan methodology for a CRS village bank of 50 members is as follows:

The maximum loan amount for the first loan cycle is CFAF 25,000. The initial funds needed from CRS by the local NGO are CFAF 1,250,000 ($25,000 * 50$). Complementary funds equal to the savings accumulated by the membership would be needed from CRS for every new loan cycle.

(1) Cycle 1:

Loan 1 = CFAF 25,000; forced savings CFAF 5,000 (20%)

(2) Cycle 2:

Loan 2 = CFAF 30,000 (savings + loan 1); savings = CFAF 6,000

Total funds needed: CFAF 30,000 * 50 = CFAF 1,500,000

Funds already available at the NGO = CFAF 1,250,000

CRS complementary funds: $5000 * 50 = \text{CFAF } 250,000$

(3) Cycle 3:

Loan 3 = CFAF 36,000 (savings + loan 2); savings = CFAF 7,200

Total funds needed: CFAF 36,000 * 50 = CFAF 1,800,000

Funds already available at NGO = CFAF 1,500,000

CRS complementary funds: $\text{CFAF } 6000 * 50 = \text{CFAF } 300,000$

3. Lending technologies

CRS provides technical assistance to its partner NGOs on an on-going basis. Most partner NGOs do not specialize in microfinance, which is an important weakness. Thus, at least a one month effort is allocated to training NGO staff on the village banking methodology, accounting and loan management, and monitoring procedures. CRS monitors partner NGOs by requiring quarterly financial statements on all village bank operations, including internal account loans to non-members.

Village banks are formed by women who know each other well. Members attend 30 compulsory hours of education courses, once to twice a week. Sessions last one and a half hours and focus on health, literacy, numeracy, and loan management. This combination of financial and non-financial services differentiates these programs from specialized financial organizations. Village bank members meet twice a month, once for education courses and the second time for loan repayment. Solidarity group members meet more often. Only village bank members and sometimes village leaders are allowed to attend these meetings. Members who fail to attend any meeting without valid reasons or who come late to meetings are penalized and have to pay a fine.

Loan repayment relies on group monitoring, peer pressure, and group liability. Members who fail to pay their loans are pressured by others, who can visit the borrower's family members or even the village chief in an effort to get the money back. Anyone who wants to leave the village bank should pay off all her debts first. The accumulated deposits by the departing member can also be used to pay off any outstanding debt.

There is no physical collateral requirement for a village bank loan obtained from the local NGO. However, loans granted to non-members from the internal account require a guarantor who is a village bank member or physical collateral. In case of default, the group is penalized and cannot get another loan. Since the inception of the program, at least three village banks have closed due to bad performance. Any village bank member can take a "break" from the program, *i.e.*, refrain from acquiring a new loan at the end of a particular cycle, however, and rejoin the program later on.

4. Outreach

CRS believes in poverty lending and especially in targeting women. Other CRS principles include using a group-loan technology, promoting local savings, and building financial self-sufficiency. As of June 30, 1997 the CRS village banking program in Benin had 2,702 members, of whom 82 percent were women (see Table 18). The volume of loans outstanding was CFAF 44,852,376 (US\$ 89,705), for 2,313 loans with an average loan size of CFAF 40,000 (US \$ 80). The poverty index in Benin is based on income of less than CFAF 10,000 (US \$ 20) per month.

Table 18. Indicators of Outreach for the CRS Program in Benin

A. Program Characteristics	June 30, 1997
Number of partner NGOs	3
Number of village banks	59
Number of village bank members	2,702
Proportion of female members (%)	82
Number of loans outstanding	2,313
Volume of loans outstanding (US\$)	89,705
Average loan size (US\$)	80
Total savings balances (US\$)	71,104
B. Performance Indicators	
Operational self-sufficiency (%) ^a	39.7
Arrears rate (%)	22

Source: CRS reports

Notes: *a*: Operational self-sufficiency is reported is for the three partner NGOs, and it was 39.7 percent for all of their activities. It was 96 percent for their financial activities only.

5. Sustainability

The village banking program has closed several banks since its inception because of bad performance. As of June 30, 1997, repayment of outstanding loans at the functioning 59 village banks was 72 percent, with an arrears rate of 22 percent (see Table 18). Lack of operational self-sufficiency of the program implied that revenues covered only 39.7 percent of operating costs, when all activities, financial and educational, were taken into account. Operational self-sufficiency of 96 percent was claimed when only credit activities were considered (CRS-Benin *Third Annual Report*, September 1997).

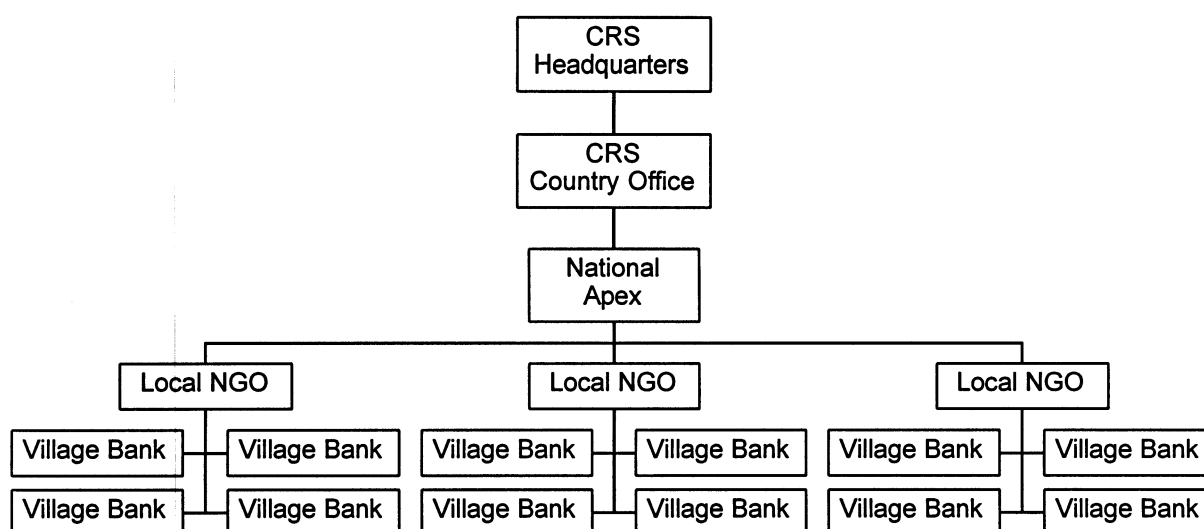
For the long-term sustainability of the program, CRS is considering the creation of an apex organization that would provide technical assistance and channel donor funds to partner NGOs. If things go according to plans, the apex organization would be created in Benin by the end of 1998, as well as in Senegal and Burkina Faso, where CRS operates similar village banking programs (see Figure 6). Creation of an apex will not correct, however, for the shortcomings and lack of sustainability of the retail organizations.

6. Ownership and governance

The CRS village banks are developed by NGOs. Most often, these NGOs do not have a clear ownership structure, and this may translate into diluted and confused ownership at the village bank level. It is not at all clear whether village bank members remain the sole residual claimants of the village bank's assets in case of dissolution.

Figure 6. CRS Village Banking Design: An Apex Model

CRS: Apex Model



E. Policy Recommendations

Several lessons and policy recommendations for the sustainability of village banking programs emerge from this case study:

- (a) *Voluntary* deposit mobilization should be emphasized and forced savings de-emphasized.
- (b) An individual-loan technology should be considered in addition to group lending, and loans should not be targeted to specific clienteles or uses.
- (c) NGOs implementing village banking programs should realize that building a financial institution is a long-term process that requires several years of intense cooperation.
- (d) Ideally, a support facility should be in place before the sponsoring agency leaves. This facility would be in charge of providing continuous technical support and auditing services.

The main remaining issues concern ownership and governance. These issues are still an open question in village banks and even in the *caisses villageoises*. Although the CVECAs have successfully dealt with the ownership and governance issues so far, there is still concern as the *caisses* grow outside of their village settings. What will happen when the village structures change or the *caisses villageoises* move to a more urban environment, where family ties and other traditional arrangements of social cohesion no longer exist? Will the *caisses villageoises* restrict themselves to a village environment that suits them best or will they adopt a new organizational form to address new concerns of ownership and governance in less hospitable settings?

The PARMEC law governing mutualist organizations also remains an important unresolved issue. What will organizations like the village banks, in their present form, do? The most dangerous provision of the PARMEC law remains the cap on interest rates that these organizations can charge on their loans. At present, the ceiling rate would not allow microfinance organizations, especially those newly created, to be sustainable. Hopefully, as the law is tested in the field, it may induce lawmakers to revise it in the direction that would benefit all microfinance organizations.

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Annex A

Contact for Village Banking Study

Caisses villageoises, Mali:

Adama Kodio, Director, Service Commun
Daniel Saye, Officer, Service Commun
Moctar Yellcouye, Officer, Service Commun
Malick Tembely, Officer, Service Commun

Freedom from Hunger and Kafo Jiginew, Mali:

Aminata Ballo, Manager, Village Banking Program
Sidiki Kone, General Inspector, Kafo Jiginew
Peggy Roark, Freedom from Hunger, USA
David Dao, Kafo Jiginew

Save the Children, Mali:

Aboubacar Konate, Administrator; Sahel Field Office in Bamako
Jeff Ramin, Technical Advisor
Barnabe Diarra, Project Coordinator, Kolondieba
Amadou Diarra, Coordinator, Village Banking Program
Ahoua Toure, Vice-manager, Village Banking Program

Catholic Relief Services, Benin:

Ange Tingbo, Catholic Relief Services, Benin
Anne Sellers, Project Administrator, Cotonou